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Note by the Secretary-General

The Secretary-General has the honour to transmit to the Security Council the report of the Board of Auditors on the financial statements of the United Nations Compensation Commission for the biennium ended 31 December 2003 (see attachment).

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Attachment

REPORT OF THE BOARD OF AUDITORS TO THE SECURITY COUNCIL ON THE FINANCIAL STATEMENTS OF THE UNITED NATIONS COMPENSATION COMMISSION FOR THE BIENNIUM ENDED 31 DECEMBER 2003

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Chapter I

Financial report for the biennium ended 31 December 2003

Introduction

1. The Secretary-General has the honour to submit herewith the financial report on the accounts of the United Nations Compensation Commission (UNCC) for the biennium ended 31 December 2003. The accounts consist of three statements and notes to the financial statements. The financial statements and the notes thereon are an integral part of the financial report.

Background

2. The United Nations Compensation Commission is a subsidiary organ of the United Nations Security Council. It was established in accordance with Security Council resolutions 687 (1991) and 692 (1991) to process claims and pay compensation for direct losses and damage suffered by individuals, corporations, Governments and international organizations as a direct result of Iraq's invasion and occupation of Kuwait (2 August 1990 to 2 March 1991).

3. The Commission is composed of the Governing Council, panels of Commissioners, and the secretariat. The Governing Council is the policy-making organ of the UNCC. Its composition is the same as that of the fifteen-member Security Council at any given time. The Governing Council makes decisions on recommendations made by the panels of Commissioners regarding compensation for claimants. The panels of Commissioners review and evaluate the claims submitted by Governments on behalf of their nationals, their companies or on their own behalf. On the basis of their review, which is undertaken in instalments of claims, the panels recommend compensation awards to the Governing Council. The secretariat, headed by the Executive Secretary, services and provides assistance to the Governing Council and the panels of Commissioners.

Operations

4. Since inception, more than 2.6 million claims have been received by the Commission within the filing deadlines. To date, the Commission has resolved over 98 per cent of the claims submitted, consisting of the claims of individuals for departure from Kuwait or Iraq (category "A" claims), the claims of individuals for serious personal injury or death (category "B" claims), the claims of individuals for losses up to US$100,000 (category "C" claims), the claims of individuals for losses over $100,000 (category "D" claims), the claims of corporations, other private legal entities and public sector enterprises (category "E" claims), and the claims of Governments and international organizations (category "F" claims). The Commission has resolved all category "A", "B" and "C" claims, save for Palestinian "late filed" claims in category "C" that are currently being processed.

5. Claims resolved to date have been awarded compensation amounting to approximately US$48 billion. As at 31 December 2003, the Commission has made available to Governments and international organizations approximately US$18 billion for distribution to successful claimants in all categories. Funds to pay compensation are drawn from the United Nations Compensation Fund,

which receives a percentage of the proceeds generated by the export sales of Iraqi petroleum and petroleum products. This percentage was originally set at 30 per cent by the Security Council under its resolution 705 (1991), and was maintained in Security Council resolution 986 (1995) which established the "oil-for-food" mechanism and in subsequent resolutions, extending the mechanism. The percentage was reduced to 25 per cent as of December 2000 by Security Council resolution 1330 (2000). The Security Council in resolution 1483 (2003), adopted on 22 May 2003, reduced the percentage further to 5 per cent.

6. Under the Temporary Payment Mechanism contained in decision 197 (2003) of the UNCC Governing Council, payment of compensation awards was limited to US$200 million following each session of the Council to take account of the reduced level of income to the Compensation Fund arising from the adoption of Security Council Resolution 1483 in May 2003.

Financial overview

7. The Compensation Fund is operated in accordance with the Financial Regulations and Rules of the United Nations and finances the administrative costs and payments of compensation awards decided by the Commission. During the biennium 2002-2003, income to the Compensation Fund amounted to US$3,686.6 million. This compares to a level of $8,340.7 million in the previous biennium. The reduction is due to the reduction in the percentage share of Iraqi petroleum sales referred to in paragraph 5.

8. Expenses during the biennium 2002-2003 amounted to $3,750.0 million, comprising compensation awards of $3,656.1 million, administrative expenses of the Commission of $87.7 million, and $6.2 million related to other expenses. This compares to total expenses of $9,613.6 million in the previous biennium, comprising compensation awards of $9,532.3 million and administrative expenses of the Commission of $81.3 million.

Chapter II
Report of the Board of Auditors

Summary

The Board of Auditors has reviewed the operations of the United Nations Compensation Commission (UNCC) at its Headquarters in Geneva. The Board has also audited its financial statements for the biennium ended 31 December 2003.

The United Nations Compensation Commission expenditure was $3.6 billion for the biennium. In its report on the 2000-2001 financial statements (A/57/5), the Board had focused on: awards to be paid; expenditure related to staff, consultants and commissioners; and internal controls.

The Board's main findings are as follows:

(a) The claim-processing performance of UNCC has been globally acceptable in regard to international practices, although the Board was not is a position to ascertain that it had always and in every respect been undertaken fully in line with international practices;

(b) UNCC still had no proper assurance that past payments fully reached the claimants, but expected the newly-requested audit certificates to provide it;

(c) The Board regrets that more internal audits could not be accomplished due to insufficient audit staffing by the Governing Council, and is concerned by the method used by the Governing Council, beyond the control of OIOS, to approve one internal audit position in 2000 and then to withhold authority to encumber the funded position until January 2005.

The Board recommended principally that UNCC conduct a joint risk-assessment with the Office of Internal Oversight Services; request all paying Governments and agents to provide updated information on their compensation payment system; provide the Office of Internal Oversight Services with appropriate internal audit posts; establish an audit committee, and take steps to ascertain oversight and archiving continuity after the completion of its mandate. By July 2004, the Administration planned to implement a number of appropriate remedies.

A list of the Board's main recommendations is provided in paragraph 13 of the present report.

A. Introduction

1. The Board of Auditors has audited the financial statements and reviewed the operations of the United Nations Compensation Commission (UNCC) for the period from 1 January 2002 to 31 December 2003 in accordance with General Assembly resolutions 74 (I) of 7 December 1946. The audit was conducted in conformity with article VII of the Financial Regulations and Rules of the United Nations and the annex thereto, the common auditing standards of the Panel of External Auditors of the United Nations, the specialized agencies and the International Atomic Energy Agency and the International Standards on Auditing. These standards require that the Board plan and perform the audit to obtain reasonable assurance as to whether the financial statements are free of material misstatement.

2. The audit was conducted primarily to enable the Board to form an opinion as to whether the expenditures recorded in the financial statements for the biennium 2002-2003 had been incurred for the purposes approved by the Governing Council of UNCC, whether income and expenditure were properly classified and recorded in accordance with the Financial Regulations and Rules; and whether the financial statements presented fairly its financial position as at 31 December 2003 and the results of the operations for the period then ended. The audit included a general review of financial systems and internal controls and a test examination of accounting records and other supporting evidence to the extent that the Board considered necessary to form an opinion on the financial statements.

3. In addition to the audit of the accounts and financial transactions, the Board carried out reviews under Financial Regulation 7.5 of the United Nations. The reviews concerned the financial control and internal oversight functions, the management of claims processing, the Information and Communication Technology (ICT) strategy and in general the administration of the Commission. Audit reports of the Office of Internal Oversight Services Audit have been carefully taken into account.

4. The audit was carried out during the biennium at UNCC Headquarters in Geneva.

5. The Board continued its practice of reporting to the Administration the results of specific audits in management letters containing detailed observations and recommendations. This practice helped to maintain an ongoing dialogue with the Administration.

6. Until the biennium 2000-2001, income and expenditures were included within the financial statements of the United Nations (Statement XII). The Board's findings and recommendations were thus disclosed in its report on the United Nations (A/57/5) which will be quoted here as 'the Board's previous report".

7. In its report A/57/439, the Advisory Committee on Administrative and Budgetary Questions (ACABQ) "*noted from paragraph 14 of the report of the Board of Auditors that the total income given for the United Nations for the*

biennium 2000-2001 of $12.95 billion includes $8.34 billion (64 per cent) of the United Nations Compensation Commission. The Committee is of the opinion that combining the income and expenditure of UNCC with that of the United Nations distorts the financial position of the United Nations. The Committee therefore recommended that the financial statements and schedules of UNCC be prepared separately and be reported on by the Board for consideration by the Governing Council of UNCC".

8. The UN General Assembly implicitly endorsed this option in its resolution A/RES/278 covering *"the observations and recommendations contained in the report of the ACABQ"*. The United Nations Secretariat subsequently informed the Board that the audited financial statements of the UNCC would be submitted "to the Security Council, as its parent body", and that they would be "public" as was the case under the previous format. This is the context in which the Board is presenting this report on the financial statements for the biennium 2002-2003.

9. The present report covers matters that, in the opinion of the Board, should be brought to the attention of the Security Council. The Board's observations and conclusions were discussed with the Administration, whose views have been reflected in the report, to the extent possible.

10. A summary of the Board's main recommendations is contained in paragraph 13 below. The detailed findings are discussed in paragraphs 15 to 203.

1. Previous recommendations not fully implemented

11. In accordance with General Assembly resolution 48/216 B of 23 December 1993, the Board reviewed the measures taken by the Administration to implement the recommendations made in its report for the biennium ended 31 December 2001(A/57/5 Vol. I). Details of action taken and the comments of the Board are included in the report and have been summarized in the annex to the present chapter. Out of a total of 10 recommendations, 6 (60 per cent) were implemented, 2 (20 per cent) were under implementation and 2 (20 per cent) were not implemented.

12. The Board has reiterated, in paragraphs 126 and 199 of the present report, previous recommendations that had not yet been implemented. The Board invites the Administration to assign specific responsibility and establish an achievable timeframe to implement them.

2. Main recommendations

13. The Board's main recommendations are that the United Nations Compensation Commission:

(a) **Reconsider its decision not to request Member States to include in every audit certificate a comprehensive and up-to-date information on their national compensation payment system, and ensure accountability by a recipient country for payments made to and by them after the termination of UNCC (para. 112);**

(b) **Prepare in conjunction with the United Nations Secretariat appropriate oversight mechanisms on compensation payments after the termination of the present structure (para. 113);**

(c) **Conduct a joint risk-assessment with OIOS, so that a proper audit plan be developed, considering that award decisions and payments are still to be made for billions of dollars (para. 126), and follow-up appropriately on internal audits (para. 146);**

(d) **Consider the appropriateness of establishing an audit committee in the context of its final operations (para. 147);**

(e) **Take, with the United Nations Secretariat, appropriate steps for the long-term management, guardianship and streamlined retrieval of archives, after seeking, in compliance with the United Nations Financial Rule 106.11, the agreement of the Board of Auditors on the period after which they may be destroyed (para. 188 & 194).**

14. The Board's other recommendations appear in paragraphs 46, 56, 72, 117, 157, 164, 184, 196, 199 and 203.

B. Background

15. The Security Council's resolution 687 (1991) established the Commission to determine and resolve claims, and administer the Compensation Fund whereby such claims would be satisfied from monies provided by Iraqi oil sales. The Commission comprises three components. A Governing Council (Member States' representatives in Geneva) is responsible for setting the policy regarding the Compensation Fund, the procedures applicable to claims resolution, and deciding upon awards to be made. Panels of commissioners (outsourced consultants) apply the procedures and recommend awards to the Council. Finally, a Secretariat assists them. The experts of the Panels were to provide "some element of due process" from a legal viewpoint, as indicated by the Secretary General of the United Nations in a 2 May 1991 report to the Security Council.

16. The Governing Council is composed of the same Member States as the United Nations Security Council, and it reports on its activities directly to that body after each session. Like most international governing bodies, it consists of diplomats representing Member States, at the United Nations Office at Geneva. It has adopted in 1992 Provisional Rules for claims procedures in which it allowed itself "to review amounts recommended (by the Panels) and, where it determines circumstances require, increase or reduce them" (Article 40 (1) of the UNCC Rules).

17. The Panels consist of "experts on mission" in accordance with United Nations Regulations and Rules. They are chosen for their professional qualifications, experience, integrity as well as geographical representation. As set out in Article 18 of the Provisional Rules For Claims Procedure (S/AC.26/1992/10), the Secretary General requested Members States of the

United Nations to provide lists of their most respected and internationally renowned candidates. The Secretary General then nominated candidates for approval by the Governing Council on the basis of recommendations from the Commission's Executive Secretary. Members of the Governing Council may have recourse to their own national experts, to review and provide questions on the reports submitted by the panels of Commissioners.

18. Since its inception and as at 7 May 2004, UNCC has resolved 2.6 million claims, i.e. over 98 per cent of the claims submitted. It had awarded compensation of $48 billion, while the related claimants had sought a total amount of $266 billion. Ninety-six Governments had filed all claims on behalf of their nationals, corporations and themselves. Thirteen offices of three international organizations filed claims on behalf of individuals not in a position to submit their claims through a Government.

Table II.1

Claims awarded, cumulative as at 7 May 2004

(Thousands of US dollars)

Category	1. No. of claims resolved	2. Compensation sought by claims resolved (Th. dollars)	3. No. of resolved claims awarded compensation	4. Compensation awarded (Th. dollars)	5. Paid as at 7 May 2004 (Th.dollars)
A	919,704	3,451,526	856,170	3,190,864	3,204,244
B	5,734	20,100	3,941	13,450	13,450
C	1,662,500	8,901,796	634,376	5,011,886	5,006,879
D	9,948	7,605,969	8,717	2,513,832	2,147,003
E	6108	77,948,032	3,842	26,208,522	4,869,215
E/F	123	6,122,977	57	311,283	180,072
F	365	161,941,698	271	10,920,602	2,974,448
Total	2,604,482	265,992,098	1,507,374	48,170,438	18,395,310

Source: UNCC. Categories are explained in table II.3 below.

19. The Commission awards compensation regardless of the resources available. The financial statements disclose only the awards paid or obligated from funds already available in the Compensation Fund. As mentioned in their Note 3, they do not disclose the awards approved but not yet paid or obligated, pending receipt of funds from the Development Fund for Iraq. The mandate to pay compensation awarded has distinctly coexisted with, and is not considered by the United Nations as contingent in any way on, its mandate to evaluate losses and verify the validity of claims for compensation. The Secretary-General, in his report to the Security Council that established the Commission, had anticipated that the value of claims approved by the Commission would at any given time far exceed the resources of the United Nations Compensation Fund (S/22559, Paragraph 28).

20. During the biennium 2002-2003, UNCC paid $3.656 billion to the governments of the concerned claimants and to other paying agents, a significant decrease over the previous two bienniums, as reflected in line 1 of

the table below. Accordingly, the amount of approved awards not yet paid or obligated increased to $30.1 billion as at 31 December 2003:

Table II.2

Awards and payments per biennium

(Millions US dollars)

	1996-1997	1998-1999	2000-2001	2002-2003
1. Compensation awards payments	713	5,414	9,532	3,656
2. Approved awards not yet paid or obligated	5,341	8,499	21,281	30,118

Source: UNCC

21. During the biennium, UNCC processed 8,730 claims, most of them for material amounts claimed, and awarded $12 billion in compensation:

Table II.3

Claims awarded during the biennium 2002-2003

	Category	*No. of claims*	*Awards (Millions of US dollars)*
A	Individuals *	0	0
B	Individuals, serious personal injury or whose spouse, child or parent died as a result of invasion and occupation of Kuwait **	0	0
C	Individual claims for damages up to US$100,000 each ***	883	16
D	Individual claims for damages above US$100,000 each	5,058	1,730
E	Corporations, other private legal entities and public sector enterprises	2,617	3,420
E/F	Mixed	83	277
F	Governments and international organizations	89	6,602
Total		**8,730**	**12,045**

Source: UNCC

* Programme ended in 1996

** Programme ended in 1994

*** Regular programme ended in 1999; in 2002-2003: Palestinian "late claims" programme.

C. Financial Issues

1. Financial overview

22. The Board performed an analysis of the financial position as at 31 December 2003.

Table II.4
Statement of income and expenditure, changes in reserves and fund balances for the years 1996-2003, and approved compensations not yet paid
(millions of United States dollars)

	1996-1997	1998-1999	2000-2001	2002-2003
1. Total income	1,307	5,247	8,341	3,687
2. Total expenditure	745	5,489	9,614	3,750
3. Excess (Shortfall) of income over expenditure	562	(242)	(1,273)	(63)
4. Prior-year adjustments	0.6	1	101	74
5. Reserve and fund balances, end of year	576	336	437	448

Source: UNCC

23. The Commission had received 25 per cent of the proceeds of all Iraqi export, "Oil for Food" sales of petroleum, petroleum products, and natural gas sales, from December 2000 to May 2003. The Security Council Resolution (S/RES/1483) dated 22 May 2003 decided that, effective the next day, a decrease to 5 per cent of the proceeds, which would be deposited to the Compensation Fund special account by the new Development Fund for Iraq.

24. This decision and other circumstances led to a decrease of 55 per cent in income, relative to the previous biennium: the total combined income for the biennium ended 31 December 2003 was $3.687 billion (line 1 of the above table). This included $3.423 billion from the United Nations Escrow Account established under the provisions of Security Council resolution 986 (1995) and $196 million from the Development Fund for Iraq.

25. Total combined expenditure decreased accordingly, by 61 per cent, to $3.75 billion (line 2). This included operational expenditures of $94 million, an increase of 16 per cent over $81 million in 2000-2001. The decline in the US Dollar value in Swiss Francs increased the cost of salaries and local expenses by some $4 million, as mentioned in paragraph 50. Despite the decrease by $6.6 million of commissioner and consultant fees, to $ 22.6 million, the 2002-2003 expenditures increased by $7 million (9 per cent) in real terms, excluding exchange rate effects. A decrease had initially been budgeted.

26. The above factors resulted in a shortfall of income over expenditure of $63 million, down from a larger shortfall of $1.3 billion for the biennium 2000-2001 (Table II.4, line 3).

27. Assets of $483 million exceeded liabilities of $35 million by $448 million, as at 31 December 2003.

28. By a disclaimer issued since 2002 upon a recommendation of the Board A/57/5, Paragraph 46, UNCC informs all payees (Governments and other paying agents) that payments depend on available funds and will be

implemented only as long as Security Council resolution 687 (1991) is in force, and that Iraq, not the United Nations, is liable.

2. United Nations System Accounting Standards

29. The Board assessed the extent to which the financial statements of UNCC for the period ended 31 December 2003 conformed to the United Nations System Accounting Standards. The review indicated that the financial statements were consistent with the standards.

3. Presentation of financial statements

30. The General Assembly has, in the terms of its resolution 55/220 dated 23 December 2000, requested "*The Secretary General and executive heads of funds and programmes of the United Nations, in conjunction with the Board of Auditors, to continue to evaluate what financial information should be presented in the financial statements and schedules and what should be presented in the annexes...*". The Board has thus, with regard to this resolution, conducted a preliminary review of the general presentation and disclosure in the Financial Statements for the year ended 31 December 2003.

4. Interest on compensation claims

31. As disclosed in note 3 (c) to the Financial Statements, the Governing Council decided on the principle of the payment of interest directly linked to the principal amount of awards in 1992 (S/AC.26/1992/16):

(a) Interest would be awarded from the date the loss occurred until the date of payment, at a rate sufficient to compensate successful claimants for the loss of use of the principal amount of the award;

(b) The methods of calculation and of payment of interest would be considered by the Governing Council at the appropriate time;

(c) Interest would be paid after the principal amount of awards.

32. The Board had noted previously (A/57/5 Vol. I, Paragraph 42) that on 2 March 2002 the Governing Council had concluded that the appropriate time had not yet arrived for determining the methods of calculating and paying interest. It remained unclear as to what eventually would be the total principal amount of compensation awarded by the Commission and the length of time that would be required for Iraq to pay such amounts. The Board had noted that award decisions, which are to generate such interest payments, are based on reports transmitted to the concerned Governments, stating, for example, that "the panel recommends that interest should run from the date of loss". UNCC has continued to include this statement in its documents (as for

example in the Recommendations made by a Panel of Commissioners on the late Palestinian claims S/AC.26/2003/26,18 December 2003).

33. The Compensation Commission had emphasized that, under international law and as formally accepted by Iraq, the liabilities and obligations associated with the payment of interest on compensation awards rested with the Government of Iraq, not the Commission or the United Nations as a whole. According to paragraph 16 of Security Council resolution 687 (1991), which under article 31 of the rules for claims procedures formed part of the law applicable before the Commission, Iraq was liable under international law for any direct loss, damage or injury to foreign Governments, nationals and corporations, as a result of its unlawful invasion and occupation of Kuwait. Iraq had agreed to the terms of resolution 687 (1991) on 6 April 1991, three days after its adoption.

34. UNCC confirmed to the Board that *"the issue of the methods of calculation and payment of interest should be addressed in a future session of the* Governing *Council at the appropriate time"*. By May 2004, the issue had yet to be addressed.

35. UNCC and UNHQ had further commented that the issue might disappear if the interest rate was set at "zero" per cent. Such a zero rate is not however implied by Decision 16, which decided that it would be *"a rate sufficient to compensate successful claimants for the loss of use of the principal amount of the award"*. Awards have indeed been related to loss of use of assets. This, in view of the above definition, entails a potential interest liability for the Government of Iraq but to be processed through UNCC. At standard interest rates, it would be material, amounting to billions of dollars. The Board's assessment of the overall financial position does not take into account this unquantified risk.

36. Taking note that the Governing Council has yet to agree on a methodology on interest payment, **the Board therefore wishes again, at a time when UNCC approaches the completion of its mandate, to draw attention to the lack of decision on the matter of the payment of interests on compensation awards.**

5. Compensation payments

37. The Governing Council makes compensation award decisions during four sessions a year, in accordance with "general principles decisions". UNCC certifies the amounts to be paid, and the United Nations Office at Geneva (UNOG) approves them. UNCC creates payment requests in the United Nations' Integrated Management Information System (IMIS), after verifying which countries should be suspended from receiving payment.

38. On the payment value date, the Commission sends a letter to the payee, that is in most cases the Government of the country of origin of the claimant, for information about the payment to come and the payee's obligations (reporting and deadlines in the use of funds), along with a detailed list of claims, and claimants. The Governing Council in its decision 17 (1994)

assigned responsibility for the distribution of compensation to each Government concerned. Its decision 18 (1994) required that Governments, exercising this responsibility, should report to the Commission information regarding the distribution of payment. UNCC does not receive information directly from individual claimants on when and whether they eventually received the payment; it receives reports from Governments and other paying agents on the amounts paid and the dates of payments to claimants. The information received is presented to the Governing Council at its quarterly sessions.

Suspension decisions

39. In accordance with the relevant decisions of the Governing Council, a country that fails to report the distribution of funds received from the Commission, or to return any undistributed funds by the deadlines set by the Governing Council, shall be suspended from receiving further payments. UNCC blocks further payments until the suspension is lifted.

40. There was, by May 2004, no comprehensive report on the up-to-date suspension situation of all concerned countries. There was furthermore no suspension history per country that could serve as an audit trail. The UNCC Secretariat considered that developing such reports would be of a "*high cost that far exceeds the potential benefits*". Quarterly reports are given to the Governing Council concerning up-to-date payments suspension and UNCC considers that "*they could serve as an audit trail regarding the suspension of any single country or set of countries with a little effort*". The Board is of the view that, considering the number of files to be monitored, a comprehensive report might have been appropriate in this matter.

Repayments

41. The procedure described above is applicable whether payments happen in an ordinary case or when Governments ask for payment of previously withheld amounts as soon as they have become compliant. The latter case means that UNCC also handles re-payments as an important part of its payment activities, as shown by the following figures:

Table II.5

Claims paid and re-paid, 1997-2003

	1. Number of claims paid	2. Number of claims re-paid	3. Amounts paid Col 1+2, $ billion	Staff posts in charge
1997	286,000		0.71	
1998	478,100	117	1.20	
1999	932,800	2,349	2.70	*Not*
2000	485,700	10,571	4.97	*audited.*
2001	32,300	26,974	4.09	
2002	5,400	11,888	2.40	11
2003	9,100	5,071	1.92	9
total	2,229,400	56,970	17.99	

Source: UNCC

42. Refunds are made by a Government when it has not been able to locate a claimant. When the claimant has finally been located, the Government asks for repayment. If the refunded amount has already been written-back, a new allotment is needed. The Board found that the procedure was under control, with little or no risk of overpayment.

Payments procedure

43. There are, toward a payment, successive manual data entries, of:

(a) claims data in one database;

(b) payment method in the Claims Payment Management System database (CPMS);

(c) miscellaneous obligations numbers generated by the Integrated Management Information System (IMIS, which the Board has separately audited in several occasions);

(d) suspension status;

(e) IMIS obligation number kept in a third, Excel database to create payment requests in IMIS in the "payment phase";

(f) modified amount (in case payment amount is different from obligation amount) to create payment request in IMS;

(g) refunds in CPMS.

44. The process involves two databases and additional spreadsheet-based sources: IMIS as an accounting system, the payment management system designed for the follow-up of claims, and *ad hoc* spreadsheet files are kept by each staff member. UNCC acknowledged "that the UNCC database and IMIS could benefit from some degree of integration to avoid the risks arising from the re-entry of similar data but so far the secretariat's discussions with the relevant UNOG staff have not resulted in the initiation of such integration which, if undertaken, will be both costly and complex". In the absence of a unique database, there has been a risk of erroneous re-entry of similar data (such as obligation and invoice payment numbers).

45. The Board found four category C re-payments for UNHCR Bulgaria, made in 2002-2003 against obligations raised in the same biennium in IMIS, which were not recorded in the payment database. UNCC explained that these transactions had been processed when using the inter-office voucher system that existed before the introduction of IMIS, and indicated that it would take corrective action.

Table II.6
Example of Balances to clear

PYIN number	OBMO number	Payee	Amount
20112	15933	UNHCR Bulgaria	$ 2,500
20116	15934	UNHCR Bulgaria	$ 7,500
25840	18403	UNHCR Bulgaria	$ 2,500
31664	22777	UNHCR Bulgaria	$ 2,500

46. **UNCC agreed with the Board's recommendation to correct accounting errors and to reduce the risk of such errors.**

6. Personnel expenditures

47. Staff and other personnel costs increased by 7.5 per cent over the previous biennium, to $77,721,842. Allotments were revised during the biennium to $76,957,150, which led to an over-expenditure of $764,692:

Table II.7
Expenditure report, 2002-2003
(United States dollars)

Expenditure line	Allotments	Expenditure report	Uncommitted allotment balance
1. Staffing table posts	43 187 200	45 082 646	-1,895,446
2. General temporary	3 260 050	3 193 478	66 572
3. Supplementary Conf. Services	7 431 300	6 707 202	724 098
4. Consultants and experts	22 988 600	22 638 069	350 531
5. Other personnel related costs	90 000	100 446	-10,445
Total	**76 957 150**	**77 721 842**	**-764,692**

Source: UNCC

48. UNCC explained the over-expenditure by the large decline of the dollar to Swiss franc exchange rate, averaging more than 17 per cent over the course of the biennium in comparison to the budget rate initially used, while most payments were denominated in Swiss Francs. Payroll allotments are based on established standard costs, with the understanding that actual costs will vary according to the individual circumstances of each staff member.

49. UNCC estimated that the dollar exchange rate downturn alone accounted for more than $4 million in increased staff and other personnel costs, and that the actual increase between the two biennia was below 4 per cent. However, the staff decreased, by 15 per cent, from 247 members in January 2002 to 209 in December 2003. Two other main factors weighted in to nevertheless increase personnel costs. Firstly, general temporary assistance costs grew from $218,790 to $3,193,478 (line 2). This reflected the recruitment of more than 40 temporary staff members in 2003 to assist with the processing of the late-filed Palestinian claims admitted by the Governing Council in 2002. Secondly, the biennium included a $1.1 million carry-over in conference services that had not been obligated during the previous biennium.

7. Operating reserve

50. The operating reserve is appropriately disclosed in the financial statements for an amount of $135 million. It was established in accordance with paragraph 7 of the Governing Council's decision 17 (23 March 1994), to

cover at least one year's operating expenses, in order to ensure the uninterrupted continuation and completion of the processing of claims by the secretariat in the event that funds would be no longer available. In 1998, the Governing council set it at $140 million, covering the years 2000 to 2003, based on an estimate of budget requirement of $40 million per year. At the end of the biennium 2002-2003, the amount was reduced to $135 million after the deduction of a $5 million provision in technical assistance to Iraq for the review of F4 environmental claims.

51. In December 2003, the Committee on Administrative Matters (CAM) decided that the proposed budget for biennium 2004-2005 ($52 million) would be funded out of the reserve. The Governing Council confirmed this decision, which appeared to be in line with the projected agenda for closing down the Commission, as discussed in section D 7 below.

8. Liabilities for end-of-service and post-retirement benefits

52. Note 5 to the financial statements on "Liabilities for end-of-service benefits" discloses $5.2 million in liabilities:

(a) After-service health insurance: the net actuarial valuation of post-retirement benefits amounts to $494,000; the Commission has limited it to four staff members, due to retire before it expects to close down; the other liabilities would be for the next employer of the some 200 other staff members;

(b) Payments for "unused vacation days", estimated at $1.6 million;

(c) Repatriation grants and related expenditures of relocation upon termination, estimated as of 31 December 2003 at $ 3.1 million.

53. The note includes Termination indemnities estimated to be not in excess of $5.05 million at 31 December 2003, for when contracts are terminated for the staff separating from UNCC in the coming years. UNHQ and UNCC announced that they would review this matter.

9. Accounts payable

54. Accounts Payables in respect of 'Undistributed funds to claimants" amounted to $9,440,659 whereas footnote e/ to the Financial Statements stated $9,438,360. Some items were still registered as payables although they should have been transferred to "prior period savings" ($8,985), a line that should then have amounted to $74.319 million instead of $74.310 million.

10. Unliquidated obligations (ULOs)

55. Unliquidated obligations amounted to $8,631,174 for the executive office and $3,364,407 for claims payments. Out of $348,541 in unliquidated

obligations related to staff termination, $295,026 had in fact been disbursed during the biennium when the shipments of personal effects had been completed. UNCC agreed that the latter amount overstated unliquidated obligations by as much.

56. **The Board recommends that UNCC review and close unliquidated obligations in a timely manner.**

11. Write-off of losses of cash, receivables and property

57. The Administration informed the Board that there were no write-offs during the biennium.

12. Ex gratia payments

58. UNCC informed the Board that no ex gratia payments had been made during the financial period ended 31 December 2003.

D. Management Issues

1. Claim and award processing

59. The Board reviewed for the present report a sample of claims that amounted to $556,425,075, with resulting awards set at $30,952,542 (Re. the breakdown by categories in annex II). The Board reviewed whether UNCC had followed its own rules and guidelines, as well as international best practices, regarding principally the information of the parties, the reviewing timeframe, the evidence, and the valuation methodologies. In so doing, the Board was aware that professional opinions on issues such as valuation methods are not internationally uniform.

Information of the parties

60. The files sampled by the Board reflected proper compliance with the Rules, especially regarding notifications to the claimants and the Governments, including that of Iraq. The Website guaranteed that all parties and the general public could have an easy access to the same data. The representatives of Iraq were involved in the steps set by the rules in this regard.

Claims reviewing delays

61. Most claims were submitted during the period 1992 to 1994. On one hand, the Categories D, E and F – large claims - were processed, individually, from 1997 to 2004. The average delay approached seven years, while the

delays generally observed on isolated claims concerning major losses are closer to some three years.

62. On the other hand, the average delay was close to those observed in similar "mass claim process" cases. This situation may be explained by the very large number of claims, the priority given to Categories A, B, and C – smaller claims - processed between 1994 and 1997, as well as by the limited operational funding, and therefore staffing, available between 1991 and 1995. The obligation to have the claimants' correspondence forwarded through the Governments was also a factor.

63. Overall, the chronology of claim filing, registration and processing of claims as reported by UNCC was in compliance with its Rules and Standard Operational Procedures.

Evidence

64. The submission of documents was based on Provisional Rules for Claims procedure article 35 and 36: "*Each claimant is responsible for submitting documents and other evidence which demonstrate satisfactorily that a particular claim or group of claims is eligible for compensation pursuant to Security Council resolution 687 (1991). Each panel will determine the admissibility relevance, materiality and weight of any documents and other evidence submitted*". The documents required were generally in compliance with international best practices.

65. Claimants may have been unable to gather the evidence requested by UNCC after several years. Not many claims included surveys, photos or videos, or statements established by the claimants shortly after the damage. UNCC attributed this to the fact that many claimants may have ignored the existence of the Commission, or have been doubtful about their chance to be compensated; therefore, they would not have constituted a claim file, originally.

66. Arguments to the contrary are that the Commission was created promptly; that all Governments were quickly informed of its existence and carried out a census of potential claimants; that claimants could otherwise ask for any kind and any source of compensation (Governmental aid, insurance companies, and direct action against Iraq) and would in such cases have constituted similar claim files.

67. The methodology took into account the lack of evidence, in the context of the war that gave rise to the claims. The consequence of that approach is that the claims seem to have been reviewed in most cases without "material evidence". It is therefore difficult to consider that the awards corresponded strictly to the reality of damages alleged by the claimants.

Valuation methodologies

68. The Principle of "mass claim processing" concerned some 15,000 claims, most of them seeking over $100,000. The choice made by the Commission to apply "general criteria" on smaller or larger groups was in

compliance with good practices. No single document was used as a reference framework for the Governing Council, the Panels, the consultants and the staff. Some Panels' reports referred to prior recommendations by the same or other Panels. This did not, however, guarantee a consistent approach to all similar claims, for which a reference tool would have been useful.

69. UNCC considered that there was a "general guide" described in Article 31 of the Provisional Rules For Claims Procedure (S/AC.26/1992/10), which provides that in "considering the claims, Commissioners will apply Security Council resolution 687 (1991) and other relevant Security Council resolutions, the criteria established by the Governing Council for particular categories of claims, and any pertinent decisions of the Governing Council. In addition, where necessary, Commissioners shall apply other relevant rules of international law".

70. The Governing Council also established precise criteria on certain legal and valuation issues, for example, on compensation for business losses: types of damages and their valuation (S/AC.26/1992/9), losses resulting from Iraq's unlawful invasion and occupation of Kuwait where the trade embargo and related measures were also an issue (S/AC.26/1992/14).

71. The methodologies have been maintained by claims categories and processing groups, considering that claims with significant common legal and factual issues were processed together. There was however no general guide providing a single document detailing the criteria and methodologies it has applied, which might be useful for archiving purposes.

72. **The Board recommends that UNCC compile a single document detailing the criteria and methodologies it has applied, for archiving purposes.**

73. The "methodologies" include a combination of valuation and adjustment techniques. They comprise "jurisprudence decisions" of the Panels or the Governing Council, on points like dates of submission, interpretation of the Security Council Decisions, delays and evidence.

74. Among the techniques are "Risk Factors" applied to claimed amounts according to the level of evidence. The valuation and adjustment techniques used in the Board's sample were in compliance with usual international practices, such as depreciation tables (applied on real estate, tangible property, stocks), valuation based on financial statements for loss of profit calculation and of income.

75. The decisions appeared to be generally satisfactory and in compliance with usual practices. Regarding the level of evidence, the Board noted that for a claim of some $609,000 the Commission's experts had considered that (i) "the claimant should supply documentary evidence confirming that the goods were not received by the buyer, such as a confirmation from the shipping company that the goods were discharged, and from the buyer, that the goods were not received"; and that (ii) eight potential sources could be consulted to

double-check that the claimed loss had not been already compensated by a third-party.

76. UNCC had noted in the file that "the Claimant has not responded to Article 34 requests". UNCC stated that the fact that a claimant did not respond to requests for additional information issued pursuant to Article 34 of the Provisional Rules was not considered by the Panels of Commissioners as a reason not to compensate a claimed loss. In such circumstances, the Panels of Commissioners would review the claim "as is", including information on the general position of similarly situated claimants; this would give rise to either a recommended award or a recommendation of no compensation. In the above claim, the Governing Council awarded the full amount.

77. Considering the large number of claims and the obligation for the Commission to work with total transparency, equity and reasonable delays, the application of "Risk Factors" as determined by the Panels and applied by the Teams seemed acceptable.

78. In view of the above, the Board was not however in a position to ascertain that the claim review had always and in every respect been undertaken fully in line with international practices.

Cross-checking

79. UNCC was required to try and identify, as much as possible, double claims, concerning for example the same party submitting a Category C and a Category D claim for the same damage, or a seller and a buyer submitting a claim for the same goods. A few sampled files reflected a lack of certainty in this respect, when only mentioning "Potential duplication of claims" without verification; or "there is no evidence of multiple recoveries although cross-checks should be made against". UNCC explained that they were extremely vigilant on the issue of cross-checking, but that cross-checking information was not always recorded on an individual claim file.

80. The distribution of the claims between the teams, and the fact that many consultants employed were based abroad, may have impaired the cross-checking work. Moreover, the methodological documents provided no guidance on this respect. The UNCC Secretariat performed the initial procedures of search and review for the Panels.

Other possibilities of compensation

81. UNCC systematically required from the claimant a statement confirming he did not "beneficiate of any other compensation from any source". UNCC and its consultants appeared to have generally considered that the claimant's statement was sufficient, while best practices would dictate to consider that a single statement might be insufficient to acquire the certainty that the claimant did not seek a double compensation.

82. The files also reflected the assumption that all insurance policies had included a war damage exclusion clause, while numerous policies, in export credit or goods in transit, do include war damage cover.

83. In most sampled cases, including large and complex claims, the consultants did not make further verification. In several cases, the possibility of an insurance cover was not analysed, even in one case where the claimant included a copy of his insurance policies. UNCC considers that Governing Council decision 13 on further measures to avoid multiple recovery of compensation by claimants (S/AC.26/1992/13) addressed this issue in several ways. Paragraph 1 requests the Government of Iraq "to provide the Commission with information about claims against Iraq in national courts or other fora for losses that would also be eligible for compensation by the Commission, and about compensation awarded for such claims". During the course of reviewing claims in categories "D", "E" and "F", the Government of Iraq did provide such information in certain cases. UNCC stated that, where appropriate, the relevant panel of Commissioners deducted such previously awarded compensation when it recommended awards of compensation in those cases, as required by Paragraph 3 (b) of Governing Council decision 13. UNCC also commented that more elaborate verification arrangements would have been costly and incompatible with its deadlines.

84. "Goods in transit" are generally covered by an insurance policy, subscribed by the sender, the shipping agent or the buyer. Nevertheless, for such sampled claims, the consultants did not request a copy of the insurance policy, and no information was required from the insurers, under notification or via the claimant.

85. The Board noted a few multi-million-dollar awards on the basis of evidence which might not be generally admitted in traditional arbitration instances, such as:

(a) Custom declaration dated 1999 and signed by the customs in 2000, while the loss was supposed to have occurred a decade earlier;

(b) Discrepancies in exporter licence numbers;

(c) Lack of identification of the delivery address, of bill of lading, purchase order;

(d) Full compensation for loss of the burglary of all cash and loss of stock (adjusted to the three previous years' average level) of a luxury goods shop, based on the single testimony of an employee;

(e) No certificate of origin; transport insurance undocumented; inconsistencies between admitted documents;

(f) Admission of a purchase which was to be valid only once a letter of credit was obtained, which was not the case, as pointed out by the representative of Iraq and the consultant;

(g) A case of valuation at the resale price, while experts might base it in such a case on production costs;

(h) For one E2 case, UNCC replied to the Board of Auditors that it had compensated a claim based on the fact that the goods had not entered the

region because of the 6 August 1990 United Nations embargo; according to the file, the goods were never at risk in the region;

(i) Lack of direct verification with insurers that there was no risk of duplicate compensation by UNCC and an insurer;

(j) Lack of verification (the maintenance and serviceability records of a jumbo jet operated by a major European airline were not sought for the valuation of its loss).

86. "Adjusting" a claim cannot be the result of a straightforward calculation. It can only reflect the experts' opinion and decisions, based on their experience. Nevertheless, the Board of Auditors also noted that between January 2001 and April 2004, the Office of Internal Oversight Services (OIOS) issued ten internal audit reports on claims awarded or recommended by the Panels of Commissioners to be awarded by the Governing Council.

87. OIOS reviewed a sample of planned awards of claims amounting to $2.2 billion, out of a total compensation sought for approximately $12 billion. The OIOS objectives were to review if there were adequate controls to ensure compliance with decisions of the Governing Council and if the compensation awarded adhered to the methodology established by the Panels. OIOS checked the "compensability", the valuation and verification of the asserted losses, the supporting evidence and the recommendations of the Panels on the compensation to be awarded.

88. OIOS found financial errors or questionable valuations, excluding some overpayments which could not be estimated (Re. annex III). Findings related to inappropriate exchange rates and depreciation rates, inappropriate accounting practices, uncertainty about the risk of overlapping claims or incorrect application of prices, insufficient evidence to support claims, inconsistent application of valuation methodologies. UNCC's response to OIOS's audit downsized the amount of planned compensation by $3.35 million, for which it cancelled the planned expenditure.

89. OIOS recommended that another $657 million in compensation be reconsidered. UNCC however considered that this recommendation fell outside of the scope of the audit, for reasons explained in section 5 below, and did not act upon them.

90. The Board's review took into account such overall indicators as the average claim processing timeframe, the "recovery rates" (percentage awarded as compared to the amount claimed) by category and instalment, the economic context and parameters.

91. The Board also noted the generally high level of professionalism of the consultants and commissioners, as well as that of the replies provided by the UNCC staff to its observations.

92. **The Board's conclusion, within the stated limits of the sample reviewed and in view of the complexity of the methodology applicable to such claims, is that the claims reviewed were generally processed in compliance with the Governing Council decisions, the rules and**

guidelines in place, and international practices generally applied for mass processing. However, the Board noted instances in which further verifications might have been beneficial.

2. Control of the distribution of funds

Government reports

93. The Commission transfers the awarded funds to the Member State Governments, principally, and to other paying agents (international organizations) that originally submitted or transmitted the claims. Those Governments and paying agents are responsible for the payment to the successful claimants. They are required to report not later than three months after the expiration of the time limit for the distribution of each payment received from the Commission, and to refund to the Commission the undistributed compensation awards. UNCC has closely monitored the reports. It submits quarterly reports to the Governing Council on them.

94. As at 31 December 2003, for the 2.1 million claim payments distributed to them, Governments and paying agents had reported actual payments under different formats: 67 per cent of claims payments in electronic format (compared with 60 per cent as of December 2002), 3 per cent in paper format, entered into the database by UNCC (compared with 5 per cent); and 30 per cent (compared with 35 per cent) under summary reports, without details on claims and in such a way that very little data could be entered and monitored.

95. The latter percentage should be viewed in light of the Board's concern previously expressed in A/57/5 (Vol. I), Paragraph 58-61, about the lack of a mechanism to ensure that the funds actually reach the intended claimants. The Board had recommended that UNCC monitor the number of distribution reports recorded manually in its database and the number of reports requiring significant reconciliation work, with a view to assess its workforce requirements. UNCC's secretariat believes that it would be impractical to devise criteria to group reports that require "significant" reconciliation work, and that the volume of correspondence exchanged with Governments may be used to supplement its workload indicators.

Field visits

96. In the light of Governing Council decisions 17 and 18, UNCC has not actively sought to confirm actual payments to beneficiaries during field missions. The Commission's staff has made few field missions over the years (five before 2002; only two in 2002 and one in 2003). These visits have been limited to a review of national systems of payment and reporting procedures, without confirming actual payments to beneficiaries, even on a sampling basis.

97. After an interim audit, which led to mention that joint OIOS/UNCC inspection missions might carry out regular field inspections of payments

made to claimants, the Working Group of the Governing Council concluded that the issue of joint inspection missions may again be reviewed should the need arise.

Audit certificates

98. The Office of Internal Oversight Services had recommended in 1998 and 2001 that the Commission require Governments and other paying agents to provide audit certificates relating to payment reports. In 1998, the Working Group of the Governing Council had not seen fit to submit this recommendation of the Office of Internal Oversight Services to the Governing Council. In 2000, the Governing Council considered the renewed recommendation submitted by the Secretariat, but did not accept it. The Board then noted in its previous report A/57/5 (Vol. I), Paragraph 62, that the Executive Secretary had again, upon its recommendation, informed the Governing Council in May 2002 that such audit certificates, and field inspections should help to provide further assurance that the funds transferred to Governments and international organizations for distribution to claimants actually reach the intended recipients.

99. The Board had also recommended A/57/5 (Vol. I), Paragraph 61, that UNCC establish a policy requesting Governments and other paying agents to provide audit certificates. The Board had noted that this is a frequent practice for most nationally- executed expenditures financed by the United Nations system and the specialized agencies, as an essential part of the accountability system.

100. The Board is pleased to note that the Governing Council eventually decided at its 49th session (18 September 2003) to request such audit certificates, covering payments after that date. The audit certificates are expected to be provided by the Member States' audit institutions.

101. The UNCC Secretariat's view on the $18 billion already paid is "*that audit certificates would have served a more useful purpose had they been required from the beginning of the payment process. At this stage, when nearly all claims have been paid in full and reported as distributed, the certificates are of marginal utility. Besides, most of the claims remaining to be paid tend to be high value claims and we expect that the claimants involved are better placed to ensure receipt of their awards.*"

102. While concurring with the above statement, the Board is of the view that for the $30 billion in compensation awards not yet paid as at December 2003 the forthcoming audit certificates if properly established and reviewed, will increase the level of accountability. In addition, they are to cover payments related to future awards.

103. The decision was notified to all Governments and Specialised Agencies participating in the payment process in September 2003. It allowed Governments to provide audit certificates annually, no later than 3 months after the end of the calendar year. The first certificates were therefore not yet

due at the time of the Board's 2004 audit, and the secretariat had not received many of them.

104. Six years elapsed between the initial audit certificate principle recommendation and its eventual adoption by the Governing Council. The Board regrets to note that $18 billion dollars were paid by the United Nations during that period without such an assurance, due to the opposition of the Governing Council.

105. **The Board notes that UNCC still had no proper assurance that past payments fully reached the claimants, but that the newly-requested audit certificates are expected to provide assurance as of 18 September 2003.**

National compensation payment systems

106. The Governing Council decided not to require information on the national payment systems. This information would therefore be only voluntarily included: the above-mentioned audit certificate's template calls for a simple statement, with no relevant background information on payment processes, contrary to best practices or international standards on auditing.

107. By May 2004, twelve Member States had still not provided information on their national compensation payment system. The value of the related claims was $14.3 million.

108. During interim audits, it was noted that UNCC did not remind the non-compliant Governments, when the amounts involved were deemed significant, to provide the information requested by Decision 18: "prior to or immediately following the receipt of the first payment from the Compensation Commission each Government shall provide information in writing through the Executive Secretary to the Governing Council on the arrangements that it has made for the distribution of funds to claimants, and subsequently promptly report any changes to those arrangements". UNCC reminded Member States in March 2003 of this obligation, recalling that "whenever a fresh payment is made, all Notes communicating these payments do request that the information on arrangements be provided".

109. The Board regrets however that, as noted above, the Governing Council decided not to require that the national payment systems be documented and covered by the newly-created audit certificates.

110. The Board has therefore no assurance that it could rely on the forthcoming audit certificates, with regard to the national compensation payment systems, and regrets that the Governing Council did not set more demanding accountability requirements.

111. The present UNCC structure may be terminated after completing the review of all claims, but payments will continue for whatever duration and funding are decided, so will the need for proper accountability. The need for proper accountability will therefore not disappear with the present structure, while the latter's expertise may disappear when its staff is disbanded.

112. **The Board recommends that UNCC reconsider its decision not to request Member States to include in every audit certificate comprehensive an up-to-date information on their national compensation payment system.**

113. **The Board also recommends that the United Nations Secretariat, with a view to ensure continuity and improvements in accountability, (i) establish mechanisms to prepare for a full-fledged, appropriate oversight infrastructure of compensation payments after the termination of the UNCC in its present structure, (ii) including accountability by recipient countries for payments made to and by them after the termination of UNCC.**

114. As at 31 December 2003, undistributed funds returned, net of re-payments, amounted to $118.9 million, with three countries having returned and not repaid more than $25 million each. At the same time, 19 Governments were not compliant with the 9 and 6-month reporting deadlines, for a total amount of $13.6 million (an improvement over the situation as at 31 October 2002, when 24 Governments and 2 UN entities were behind schedule, for $25.6 million).

115. Payments or re-payments to non-compliant Governments are withheld pending full compliance, in accordance with Decisions dated 25 March 1999 and 30 September 1999. As at 31 December 2003, funds withheld amounted to $2.7 million, a significant improvement when compared to an amount of $38.1 million as at 31 October 2002.

116. Following an interim audit, the UNCC Secretariat now advises the Governing Council on the time elapsed in a non-compliance status, in its reports on the Distribution of Payments and Transparency and Return of Undistributed Funds.

117. **The Board commends the UNCC for the improved management of recovery of undistributed funds, and recommends that it take further action to recover undistributed funds, in view of its completion strategy.**

3. Costs withheld by Governments and Paying Agents on payments

118. Recipient Governments and paying agents had deducted for themselves a total of $190 million, by 30 November 2002, from the awards to be paid to claimants, to cover their own "Claims processing costs". This amount represented 1.2 percent of the almost $16 billion in payments made at that date. Decision 18 of the Governing Council allows Governments to offset their costs of processing claims by deducting a small fee from payments made to claimants, subject to explanations satisfactory to the Governing Council for any processing costs so deducted, to be commensurate with the actual expenditure of Governments. In the case of awards payable to claimants in categories A, B and C, the fees were not exceeding 1.5 per cent, and, in categories D, E and F, 3 per cent. No fee deduction has been rejected so far.

119. The Governing Council's working group did not decide until 11 March 2004 that a report would be produced annually to improve the control of fees. The first such report, as at 31 December 2003, showed that all reported processing fees fell within the percentage permitted by the Governing Council in its decision 18, except in the case of two category B claims where the charges were slightly higher than the maximum percentage allowed (because of bank charges not under the control of the Government).

120. The Board of Auditors requested detailed information relating to the processing costs deducted from payments made to claimants by one Government in relation with the actual expenditures for processing costs. That Government had deducted, by 30 November 2002, a total of $156 million to cover such costs. UNCC has concluded, from the information received from that Government, that "*the fees do not fully cover the costs of claims preparation and payment distribution,(...) the costs incurred in the initial period of the claims process are only covered much later when the preparations have been largely completed and payments have begun and accelerated.*". The Board is not in a position to validate this conclusion.

4. Internal oversight

Verification and Valuation Support Branch

121. The Verification and Valuation Support Branch of the Commission had a staff of 15 professionals by May 2004. This unit provided technical assistance for valuating claims, assessing, surveys and accounting reviews. It was also in contact with the external consultants and the Commissioners to build methodologies, and to review large and complex claims.

Internal audit

122. While appreciating the accomplishments of the Verification and Valuation Support Branch, the Board has been consistently of the view that a strong internal audit function was needed based on the amounts at stake. The recent findings of the internal auditors are illustrated in annex III to this report.

123. The Board had noted that under a 1997 memorandum of understanding, the Office of Internal Oversight Services assumed the internal audit function, through its Iraq Programme Section. Until 2000, audits had focused on administrative issues (contracts awarded to consultants, budgetary procedures, integrated database). The first audit related to claims was implemented in 2000 (payment procedures). Nine more audits have been implemented since then, but with only one post of internal auditor.

Risk assessment

124. The Board had recommended that the UNCC *"undertake jointly with the Office of Internal Oversight Services a risk assessment of its operations in order to determine major areas of risk in the processing of claims and payments"*. OIOS undertook a risk assessment shortly thereafter, but by itself. Both parties reached an agreement in July 2003 on the modalities of a joint assessment which, however, by April 2004, had yet to be done.

125. The UNCC Secretariat stated on 28 April 2004 to OIOS that *"a risk assessment would be of doubtful merit at this stage of play, when claims processing is due to be completed in just over half a year's time"*. The Board is of the view that the material amounts still to be processed and paid make a compelling case for an immediate, although belated, risk assessment.

126. **The Board reiterates its recommendation that UNCC and OIOS conduct a joint risk assessment, so that a proper audit plan be developed.**

Audit staffing

127. The Board had recommended in its report, A/57/5 (Vol. I), Paragraph 71, that the United Nations Compensation Commission "recognize and meet internal audit staff requirements accordingly". The Compensation Commission had provided funding for only one P-4 auditor assigned to the Office. In 2001, the Office of Internal Oversight Services requested the Commission to fund a second P-4 post. UNCC stated in the Memorandum of Understanding signed on 23 June 2003 that it "will request its Governing Council to provide funding for OIOS to establish two audit posts at the P-4 level".

128. The post for the second auditor has existed since July 2000. UNCC explained that as the Governing Council had not approved the recruitment of a second auditor, the vacant post was being used to accommodate a staff member of its own, until the Governing Council would reverse its position. OIOS indicated that it was never informed of the existence of the post since 2000 until the present report; it was informed of the possibility of a second post in July 2003. OIOS reported that it was told by UNCC that the Governing Council could not reach a consensus on staffing the second post, because one of its members felt that OIOS had yet to demonstrate its readiness to respect the scope of audit defined by the Office of Legal Affairs, but that the Governing Council finally agreed that a second auditor may be recruited as of 1 January 2005.

129. The Board notes that on one hand UNCC considered that by early 2004 it was too late to conduct an audit-risk assessment, and that on the other hand it delayed until 2005, for the final months of its claims processing, the

authority to staff the second auditor post, contrary in both cases to the Board's recommendations.

130. **The Board is concerned by the method used by UNCC, beyond the control of OIOS, to approve one internal audit position and then to withhold authority to encumber the funded position, and recalls its previous finding on this issue as reported in Paragraph 67 of its previous report (A/57/5, vol. 1).**

131. **The Board is also concerned that the Governing Council has neglected to implement the audit recommendation to increase the internal audit staffing, while the Commission's Secretariat had also recommended doing so.**

Audit scope

132. UNCC has recognised that OIOS has authority to initiate, carry out and report on any action which it considered necessary to fulfil its responsibilities with regard to its monitoring, internal audit, inspections, evaluation and investigations, as set out in the Secretary-General's bulletin ST/SGB/273 dated 7 September 1994. Both parties signed on 23 June 2003 a new Memorandum of Understanding in order to provide a sound basis for internal audit. UNCC confirmed in it that it provides "*full and unhindered access to all UNCC files and documents*" to internal auditors.

133. The implementation of the Memorandum immediately ran into problems because of the persistence of divergent views on the scope of audit. OIOS has taken the view that the compensation process resembles an "insurance loss adjustment process", for which international best practices are to have proper auditing done, and not a "judicial" or "quasi-judicial" process.

134. UNCC has indicated that it felt obliged to respect the opinion of the Office of Legal Affairs (OLA), that it was not within the proper scope of internal audit to review the admissibility, relevance, materiality and weight of the evidence supporting claims and the resulting awards, including the evidentiary standards applied by the Commission and the Commissioners for the verification and valuation of losses, on the ground that the processing of claims has a "legal" or "quasi-judicial" nature.

135. Following up on the Board's above-mentioned recommendation, UNCC requested on 22 October 2002 the advice of the Office of Legal Affairs, which replied on 27 November 2002. The Office was of the view, as stated in 1992, that UNCC was not "a court or arbitral tribunal, not judicial in nature (...) at least in major part", but that "with the exercise of this power by the panels, together with the exercise of their power to request additional written submissions, the processing of claims has increasingly assumed a quasi-judicial nature". It has also stated in other circumstances that the "Panels of Commissioners are not courts", but that the way they work is "sufficiently

judicial in character" to put their decisions and the process of their decision-making beyond the scope of audit.

136. OLA recognised that UNCC procedures did not "conform to the usual patterns that apply in the fields of either international or domestic litigation". It considered that "nevertheless they are recognisably a legal procedure (...) the fact that a procedure is not formally judicial or arbitral in nature does not mean that it is not a legal process", and that "it should be the function of the commissioners to provide that element". The "legal process" or "procedure" character was enunciated as preventing the internal audit of the "decision-making that takes place in the course, and as an integral part, of such a process".

137. OLA therefore determined that the internal auditors were to be excluded from reviewing the application of "law", including determinations relating to the relevance, materiality and weight of evidence. UNCC referred to no legal instrument of a status – such as that of a Treaty or an explicit decision of the General Assembly or Security Council - that could qualify as a "law" providing for this exclusion.

138. OLA has also been of the view that not only the Panels but also the United Nations staff members of the Commission's Secretariat assisting the Panels are similar to officers of a Court to whom internal auditors would not have access: "the substantive assistance which the Secretariat gives to the panels in conducting those three aspects of their work equally falls beyond the proper scope of audit" (OLA, 27 November 2002 opinion). The three aspects were: identification and application of the applicable "law"; the manner in which the Panels of commissioners have organised their work; and their determinations regarding the sufficiency of evidence, including their determinations relating to the relevance, materiality and weight of evidence.

139. The internal auditor could only review the correctness of "the computation by panels of the amounts of compensation which they recommend be paid in respect of a loss which they have concluded to be compensable from the Fund".

140. The Office was also of the view that the fact that the "decisions of the panels are not, as such, legally binding, but are recommendatory in nature only" was not contradicting the above. As noted above, the Panels do not make "decisions", but "recommendations".

141. As quoted above, the Office of Legal Affairs wrote in 2002 and 2003 that the Commission's processing of claims was of a "quasi-judicial" nature. Upon further communication with the Board, the Office of Legal Affairs also stated in May 2004 its view that "it is not necessary for present purposes to characterize the procedure which panels of commissioners employ to process claims. That procedure is one which is without any exact precedent in the history of international claims settlement. However, irrespective of how it may be styled, it is clear, in view of its incorporation of the elements of the due process of law identified above, that the procedure constitutes a legal process". Its opinion was not addressing "the nature of the United Nations

Compensation Commission in general, nor did it address the nature of its Governing Council".

142. After it has reached decisions on awards, the Governing Council only corrects computation, clerical typographical and other errors. There is no appellate function.

143. In practice, the UNCC Secretariat has not considered internal audit recommendations notified in 2002-2003 when it deemed that the latter were not "amenable to audit", i.e. within the scope of internal audit as narrowed in its above considerations. This latter practice is documented in annex 3 to this report, when UNCC replies, repeatedly, to internal audit observations that "*the responsibility of panels of Commissioners to assess evidence, to make findings of fact and to identify and apply legal and equitable principles are facets of a legal process that is not amenable to audit*". UNCC referred to the provisions of the 2003 Memorandum of Understanding which stated that "*OIOS will take into consideration the opinion prepared by the Office of Legal Affairs (OLA) dated 27 November 2002 concerning the appropriate scope of such audits*" as an admission of such a limitation of scope. OIOS has disagreed with this interpretation.

144. UNCC has also commented to the Board on 28 May 2004 that "OIOS does not possess the requisite claims resolution expertise and relevant legal experience to sit in judgment of reports generated by the experts who make up the Panels of Commissioners and who, individually, can often call upon 30 to 40 years of relevant practice in their fields of work". UNCC has also commented that "the task of responding to OIOS observations has required (...) considerable time and resources (...) thereby causing the UNCC to run the risk of being criticized for performing unnecessary work" (there was, as noted, a single post provided for internal audit).

145. In accordance with the International Standard on Auditing 610 on "Considering the work of internal audit", the Board has considered the activities of internal auditing and their effect on the external audit procedure.

a) In the context of UNCC's operations, the Board placed a significant degree of reliance on the work performed by the Office of Internal Oversight Services, particularly with regard to internal controls. The Board is glad to note that, following up on several recommendations provided in its report on the biennium 2000-2001, UNCC has granted OIOS an unrestricted access to all files and data.

b)However, the Board notes that, on the basis of the legal analysis that has been summarized above, UNCC did not implement the other components of the Board's recommendation. The Administration did provide the single OIOS auditor with unrestricted access during the biennium, but denied this internal auditor the mandate and competence to "review the admissibility, relevance, materiality and weight of the evidence supporting the claims and the resulting awards, including the evidentiary standards applied by the

Commission and the commissioners for the verification and valuation of losses". This was repeatedly confirmed by the Administration's replies, as illustrated in annex III to the present report, that any such considerations made by OIOS were, in the view not only of UNCC but also of the United Nations Administration as represented by the Office of Legal Affairs, "not amenable to audit".

c) The Board notes that the Commission's payments are processed through a special account established by the United Nations. The United Nations financial rule 106.4 states that the purpose and limits of each trust fund, reserve or special account established shall be as defined by the appropriate authority, and that such funds and accounts shall be administered in accordance with the financial rules unless otherwise provided by the General Assembly. The latter has not provided otherwise.

d) The Board considers that a sound internal audit system enhances the accountability of an organization, the adequacy of its processes, and the performance of management and the reliability of the financial information. In the case of UNCC, the Board is of the view that more coverage by the internal auditors was and is still needed, as recommended by the Board in 2002. Annex III to the present report confirms such a need by providing a sample of useful findings reached by the internal auditor.

e) Turning to the proved impact of internal audit, on one hand, the Board is glad to note that, as already mentioned, UNCC properly took action when the single OIOS auditor, for annual expenditures as well as awards in billions of dollars, delivered significant savings in awards to the extent of its audit coverage allowed by the Governing Council. The earlier utilisation of a second auditor post, created in 2000 but used to other means by UNCC, might have allowed for more such savings.

f) On the other hand, the Board mentioned earlier that internal audit findings on matters pronounced by UNCC as being "not amenable to audit" have put into question over one-fourth of a $2.2 billion in awards. The Board is of the view that UNCC, its processes and jurisprudence would have gained in benefiting from such audits, either in time before making decisions on proposed awards, or to the effect of learning lessons for future awards.

146. In view of the $18 billion paid so far, of the additional $30 billion in notified awards, of the interest notified in principle as to be paid as at the date of loss, and of the claims yet to be processed, **the Board reiterates its recommendation that the Governing Council unrestrictedly provide appropriate internal audit resources and consider audit findings, particularly in regard to its processes, in the interest of accountability and transparency.**

Audit Committee

147. The Board had recommended the establishment of an audit committee, adjunct to the Governing Council, considering the size and risks of its operations. UNCC has not implemented the recommendation, considering that its Committee on Administrative Matters performs the function. The Committee is composed of the members of the Governing Council. Contrary to best practices, the Committee is not composed of members independent from management, and it does not have a written charter to address: (i) the committee's purpose; (ii) an annual performance evaluation of the audit committee; and (iii) its duties and responsibilities. **The Board is of the view that this committee does not constitute an audit committee in terms of international best practices. The Board recommends that UNCC consider the appropriateness of establishing an audit committee in the context of its final operations.**

5. Information and Communication Technology strategy

148. The Board undertook a horizontal review of information and communication technology (ICT) strategy at the United Nations and its funds and programmes. The Board's focus was on the economy and efficiency of the processes that support the ICT strategy.

149. The aggregated reported information and communication technology expenditures were $2 million for 2003 (a small portion of the more than $350 million reported per year in 2002 and 2003 by the 23 UN entities reviewed, including UNCC). These figures do not include indirect costs.

Inter-agency coordination

150. Regarding coordination, UNCC has participated in several ICT inter-agency boards and related initiatives, including the former Information Systems Coordination Committee and the Information and Communications Technology (ICT) Network. UNCC helped create and develop a task force on the adoption of open-source software in the UN system, and led the ICT Network group tasked with producing a document on Information Security, which was subsequently unanimously adopted by the HLCM for system-wide use.

151. However, like all the major UN entities, UNCC developed its ICT in relative isolation from other UN System entities, and without an ICT strategy.

152. In two significant fields, UNCC did not pro-actively seek opportunities for stronger co-ordination: data architecture, and, despite its above-mentioned role in this field, security policies.

153. UNCC developed its own formal architectures for technology and for data. The absence of United Nations system-wide information management standards (indexing, classification, definition of access rights, data cleansing, archival, etc.) has contributed to a system-wide risk of unreliable information

in potentially all areas of activity where information is shared or transferred among entities. This may require special attention when UNCC will transfer its databases before closing down.

154. The Board commends UNCC for providing impetus to inter-agency co-ordination and recommends that it pays special attention to the steps to be taken for data archiving and transfer in the context of its completion strategy.

Information security

155. UNCC did not formally document its information security policies, except for the appropriate use of Internet access and e-mail. It considered that security was implemented, in practice, at multiple levels (Network access, database access, DMS access, application access, function within the application, secure internet access) and was ultimately controlled and documented via Help Desk Requests (HDRs), which were kept for archival purposes.

156. Although valuable, these do not form security policies, while, due to its size (20 posts in 2002-2003), the ICT function faced specific exposures and risks. In terms of information security, it lacked some of the resources to follow external events and to always install promptly updates, patches and fixes for software vulnerabilities. At a time of staff downsizing and activities phasing-out, this situation may present specific risks.

157. **The Board recommends that UNCC pay special attention to its information security until it closes down.**

Strategic documents and tools

158. Regarding its ICT strategy components, UNCC provided the Board with a work plan dated 1998 and budget proposals up to 2003. The documents available did not, however, include a number of standard items, such as estimated costs or quantitative benefits expected from investment plans.

159. The ICT organization has delivered the necessary systems and facilities, but without abiding by some significant best practices, and without benchmarks available to determine if this was done in the most effective manner.

Standards

160. UNCC did not adopt either of the two formal standards relating to ICT matters that have been in use for many years (ISO 9001 for Total Quality Management and ISO 17799, a Code of Practice for the Management of Information Security). UNCC did not adopt either ISO 17799, a model for managing information security. It also does not use the COBIT (Control Objectives for Information Technology) set of guidelines – nor a formal international standard. By not adopting any established standards, it has not been in a position to properly deliver self-assessments and management reviews of ICT.

161. UNCC has also not adopted a set of operational best practices for ICT, such as for example the Information Technology Infrastructure Library (ITIL) first published by the UK Government Central Computing and Telecommunications Agency (CCTA) and widely used across the world. UNCC stated that "implementing the ITIL would have been expensive and unnecessary given the soundness of the procedures... used for many years".

162. Regarding evaluation, OIOS has provided rather limited internal audit coverage of ICT activities. Furthermore, UNCC could not provide examples of post-implementation benefit reviews of ICT systems. Management was therefore not in a position to ascertain that completed projects conformed to what was originally approved and that the expected benefits were achieved. UNCC has documented its ICT unit work but this cannot be considered as a substitute to post-implementation review, while significant updates of its payment management system have been ongoing through 2002-2003.

163. UNCC maintains an inventory of its ICT assets – applications, documentation pertaining to such applications and documented plans for the evolution (enhancement, replacement, abandonment) of these applications. This will be an essential support component for core systems and data after its phasing out.

164. **The Board recommends that UNCC continue to maintain its comprehensive inventory of information and communication technology assets and related supporting documentation, to ensure that their core systems and data can remain accessible and available after completion of its activities.**

6. Phasing out of the Commission's activities

165. Deadlines for the completion of claims processing and related activities were so far rescheduled by Governing Council decisions. In 2001, the completion was scheduled for the end of 2003. The work programme required more costly support than anticipated, but the deadlines had generally been adhered to, until the above-mentioned decisions added new workloads.

166. The November 2003 operational budget for the biennium 2004-2005 ($51,706,300) has set a new deadline. The final recommendations of the panels of Commissioners would be examined in June 2005. UNCC has accordingly forecast a reduction in costs of nearly 40 per cent in comparison with the biennium 2002-2003. The staff would decrease from the 230 approved posts in 2003 to 171 in October 2004 and 43 in October 2005. The budget for 2005 is $12.9 million, with no more fees for commissioners and $50,000 only for consultants.

167. At the end of 2003, UNCC relinquished 1,500 square meters in office space, and consolidated staff within the outside building's remaining space and the Palais des Nations (*Villas la Pelouse* and *la Dépendance*). The annual rental of premises would decrease from $1.69 million to below $0.9 million in 2005.

168. This budget for 2004-2005 assumed the completion by the end of 2003 of all D, E1, 2, 3 and 4, E/F and F3 claims. However, in 2004, there were still D claims to be examined.

169. A second assumption was that late claims would be decided upon by the first quarter of 2005. The Governing Council accepted at its March 2004 session 3,955 new C "late claims", although it had set a July 2002 deadline for these. It also decided to *"not consider or accept any further requests for the late filing of claims in any claims category"*.

170. The special "late claims" programme was opened in 2001 to a group of claimants stating that they had not had a full opportunity to file claims in time. The estimation was that 5,000 claims might be filed, but 46,000 were filed by the July 2002 deadline. The additional consultant fees and other costs had been projected at $16,284,850, of which 26 per cent related to 2002-2003 and 74 per cent to 2004.

171. The processing of the batch of 23,600 awards remaining to be repaid, for an amount of $90 million already obligated, could take several years. UNCC had yet to consider a deadline beyond which claimants would no longer be entitled to receive payment for their awards.

172. Another factor explaining the delaying of completion related to Article 41 of the Rules for Claims procedure stating since 1992 that *"1) Computational, clerical, typographical or other errors brought to the attention of the Executive Secretary within 60 days from the publication of the decisions and reports, will be reported by the Executive Secretary to the Governing Council 2) (who) will decide whether any action is necessary"*. With thousands of such queries received each year since 2001, eleven reports on these corrections have been submitted to the Governing council in the last three years, a higher level than anticipated in the initial phasing-out objectives. The Secretariat of UNCC was planning a revision of Article 41 by mid-2004 to address the risk of protracted queries, in order to ensure the timely and cost-effective completion of its mandate.

173. By May 2004, UNCC had yet to adjudicate claims, principally very large ones, totalling some $100 billion, and expected to reach a decision on them before the end of the biennium 2004-2005. It had processed all individual category "A" and "B" claims, and most "C" claims of individuals for losses up to $100,000. Some "D" claims of individuals for losses over $100,000, of corporations, other private legal entities and public sector enterprises ("E" claims), and of Governments and international organizations ("F" claims) were still pending, as well as the 46,000 C and D Palestinian claims.

174. UNCC was therefore considering to discontinue most or all of its operations, by downsizing to a single paying unit, as already planned in its budget for 2004-2005, or by liquidating and transferring this function to another United Nations office. The budget for 2004-2005 noted that *"arrangements will thus be required for the assumption of these*

responsibilities, and presumably these (claim payment section) staff, by another United Nation entity".

175. Management indicated that should the Security Council take a decision impacting on the future modalities of operations, disclosure would be made at that time in the financial statements. UNCC decided to fund its 2004-2005 operating expenditures out of its operating reserve, which would then be progressively depleted in explicit anticipation of closing down most or all of its operations.

176. Information provided to the Board therefore confirms that the current biennium 2004-2005 should see the end of UNCC as a claim-processing entity. It could either be reduced to a paying agent or be terminated.

177. It had made available to Governments and international organizations $18.4 billion for distribution to claimants, by 7 May 2004. The remainder to be paid amounted to $30.1 billion, interest not included. There was no formal indication as to the date at which these awards could be paid.

178. The calendar for paying claims approved but not yet paid is almost indefinite. Their total amount might exceed $40 billion, before interest. UNCC expects for 2004 an income of some $800 million from oil sales coming from the Development Fund for Iraq.

179. As an indication, since June 2003, UNCC has received from the new Development Fund for Iraq some $200 million every three months. Successful claimants in all categories have received an initial amount of $100,000 or the unpaid principal amount of the award, if less. Subsequent rounds of payments of $100,000 (or the unpaid principal amount of the award, if less) are to be made to successful claimants in all categories of newly approved claims and of claims approved at any previous session of the sessions described above, in the order in which they have been approved, until the available funds for distribution have been exhausted.

180. At such a rate, awards already notified would be fully paid by year 2034, interests not included. They could also be cancelled, should the international community exonerate Iraq from further payments to the Commission. The "Compensation" function would then fully disappear after the final settlements and repayments, but for the guardianship of the related archives.

181. As a conclusion, UNCC indicated in 2004 that it has the intention and the necessity of curtailing materially the scale of its operations in years 2004 and possibly to liquidate them in year 2005. There is more than a significant doubt about the continuation of its mandate. The related uncertainties have not been disclosed in its financial report.

182. The United Nations have learnt lessons about the liquidation of closing missions, such as those of peacekeeping operations, which could be purposefully applied. The Board notes that the Office of Internal Oversight Services usually participates in the liquidation. By contrast, UNCC has expressed doubts on the merits of involving the latter and other United

Nations offices in the phase-out planning phase, and has refrained from doing so.

183. If the phasing-out was not properly planned and implemented in liaison with all United Nations parties involved, there would be a risk of negative impact on the UN's reputation, on the costs involved and on the proper payments to all final beneficiaries.

184. **The Board recommends that the United Nations decide promptly upon the completion strategy, phases, deadlines and modalities, including:**

(a) The procedure for the liquidation of the United Nations Compensation Commission, under an appropriate authority;

(b) The transfer of remaining activities to an appropriate structure;

(c) The termination deadline for the United Nations Compensation Commission;

(d) The deadlines for rectifications, other queries and repayments concerning awarded claims, with a view to minimise costs while improving the overall accountability on the financial operations;

(e) The involvement at all stages of the Office for Internal Oversight Services.

7. Archiving

185. The Board had recommended in its previous report A/57/5 (Vol. I), Paragraph 57, that the Compensation Commission establish and implement an archiving policy. Its standard operating procedures stated in 2002 that policy decisions with respect to the archiving had yet to be taken. The Governing Council has adopted in December 2003 the general frame of an archiving policy. It includes periods of retention set to seven years from the date of full and final payments of the last claim awards.

186. The United Nations Financial Rule 106.11 states that "accounting records, other financial and property records and all supporting documents shall be retained for such periods as may be agreed with the Board of Auditors". UNCC did not seek the agreement of the Board for the above decision.

187. By May 2004, the implementation of this policy was beginning, and there was not yet a cost estimate for the seven-year period. The Compensation Commission may however be terminated before the end of such a period, a perspective which might call for a decision on the seven-year duration to be taken by the United Nations Secretariat, with appropriate prudence. UNCC has appropriately held meetings with the latter's Archive and Records Management Section.

188. **In view of the likely termination of the United Nations Compensation Commission under its present form, the Board recommends that the United Nations Secretariat review the archiving period, in consideration of all related aspects, options and timeframes, before submitting it to the Board of Auditors.**

189. The Board had recommended that the checklist of types of documents to be filed be strictly applied to ensure that all evidence in custody of third parties is returned to the Commission in order to provide a proper full audit trail in compliance with best practices (the Office of Internal Oversight Services had made a similar recommendation in 2001). The Board noted that progress was made in that direction.

190. The Board found that the UNCC Registry has operated in a reliable manner the circulation and tracking of claim and award documents. The claim files reviewed contained all the "official documents", numbered and registered in the database: original claimant file, claim review form worksheet, letters under notification to the claimant and to Iraq and the latters' responses. All files requested by the Board were promptly delivered.

191. However, the data related to the review of a claim has been kept in several and separate series, due to space and organisational constraints: claim summaries, minutes of the panel's writings, consultant's reports, panel's reports, and Governing Council Decisions. These documents are technically an integral part of every individual claim file. It appears necessary to take steps so that, after the end of UNCC activities, access to a whole file be feasible and easy.

192. The guidelines imply a 60-day limit for a claim file to remain active after the award decision, after which files should be archived. By May 2004, some files related to claims settled several years before by the Governing Council were still partly kept in various offices, including some which had been those of former staff members in charge at the time and that had left UNCC or been redeployed.

193. For the storage and archiving of "Official Documents", different choices have been adopted by the teams concerning the documents relating to the claim review, and the type of conservation of these documents. One team, for example, has kept a copy of the Claim Summary and of one report in each file, while the other teams did not.

194. **The Board recommends that UNCC take, with the United Nations Secretariat, appropriate steps for the long-term management, guardianship and streamlined retrieval of archives.**

195. The Board is of the view that the conditions of storage and archiving have not been fully safe, with regard to the confidentiality and importance of the files.

196. **The Board recommends that the UNCC review in a long-term perspective, the security and safety of its archives.**

8. Prevention of conflicts of interest

197. The Board had recommended in its previous report A/57/5 (Vol. I), Paragraph 79, that the United Nations Compensation Commission raise staff awareness of the existing conflict-of-interest clause through a specific annex to any contract; and re-examine the policy of not prohibiting staff specifically involved in the awarding process from seeking immediate employment with the claimants or their representatives.

198. UNCC has revised the staff contracts, to include specific reference to the provisions of the United Nations Staff Regulations and Rules relating to confidentiality and outside contacts, while a staff member is assigned to UNCC and after separation. This revision is welcome, but it does not fully implement the above-quoted recommendation.

199. **The Board reiterates its recommendation that the United Nations Compensation Commission raise staff awareness of the existing conflict-of-interest clause through a specific annex to any contract; and re-examine the policy of not prohibiting staff specifically involved in the awarding process from seeking immediate employment with the claimants or their representatives.**

9. Fraud and presumptive fraud

200. The Administration reported no cases of fraud and presumptive fraud to the Board for the financial period ended 31 December 2003.

201. UNCC had no comprehensive internal anti-fraud and corruption infrastructure and plan. It included a few specific anti-corruption and anti-fraud elements in different rules, procedures and internal controls. It did not have a proactive anti-fraud and corruption strategy and plan, which means that such internal risks were not properly addressed.

(a) No effective framework and co-ordination point for prevention, detection, resolution and reporting;

(b) No formal corruption and fraud risk assessment mechanism; and no corruption and fraud-prevention committee;

(c) Conducted no ethics, anti-corruption and fraud-awareness training sessions and workshops in 2003;

(d) No appropriate resolution mechanisms for reported and detected incidents and allegations of corruption and fraud (although it relied on OIOS to do so).

202. Despite the risks at stake, OIOS regrettably did not include UNCC in the entities covered through questionnaires on investigations in its report on "Strengthening the investigation functions in the United Nations" (A/58/708), in compliance with Resolution 57/282 of 29 January 2003. This resolution had called for a review of the practice involving programme managers in

investigative processes with specific attention to independence, training and proper guidelines.

203. **The Board recommends that in the context of its phasing-out, UNCC pay special attention to its fraud prevention strategy.**

E. Acknowledgement

204. The Board of Auditors wishes to express its appreciation for the cooperation and assistance extended to its audit teams by the Executive Director and staff of UNCC.

(*Signed*) Shauket A. **Fakie**
Auditor-General of the Republic of South Africa

(*Signed*) Guillermo N. **Carague**
Chairman, Philippine Commission on Audit

(*Signed*) François **Logerot**
First President of the Court of Accounts of France

9 July 2004

Note: The members of the Board of Auditors have signed only the original English version of the report.

Annex I: Summary of status of implementation of recommendations

For the financial period ended 31 December 2001 [1]

Topic	*Implemented*	*Under implementation*	*Not implemented*	*Total*	*In this report*
A. Financial issues					
Claims audit trail	Para. 55			1	189
Audit certificates	Para. 61			1	86-105
Undistributed funds		Para. 64		1	114-117
B. Management issues					
Internal control	Para. 75		Para. 74	2	121-145
Archives		Para. 57		1	185-196
Legal framework			Para. 44	1	
Staff recruitment	Para. 49			1	
Commissioners payment	Para. 52			1	
Prevention of conflicts of interest		Para. 79		1	199
Total					
Number	**6**	**2**	**2**	**10**	
Percentage	**60 %**	**20 %**	**20 %**		

[1] A/57/5, vol. I.

Annex II: List of claims audited by the Board

(United States dollars)

UNCC Number	Cat-egory	Instalm -ent	Claim amount (CA)	Award (A)	Recovery rate A/CA *
4001066	E2	10	1,641,433	41,321	3%
4005965	E2	10	87,725	27,695	32%
4000197	E2	10	6,257,500	-	0%
4000106	E2	9	640,500	124,445	19%
4001965	E2	10	228,244	154,591	68%
4001971	E2	9	1,206,944	392,015	32%
4001614	E2	10	101,809	91,628	90%
4000001	E2	1	472,833,095	16,017,276	3%
4002554	E2	14	623,731	102,699	16%
4001494	E2	12	5,523,142	593,524	11%
4001726	E2	13	147,420	147,420	100%
4002244	E2	11	2,400,000	946,320	39%
4000716	E2	12	1,185,907	-	0%
4001485	E2	7	34,931,441	625,853	2%
4002477	E2	7	891,799	-	0%
4002408	E4	1	1,826,757	781,257	43%
4002398	E4	1	155,111	79,743	51%
4000806	E4	1	871,280	622,889	71%
4000760	E4	1	342,190	238,776	70%
4004137	E4	21	1,004,259	766,786	76%
4001711	E/F	1	996,656	-	0%
4000292	E/F	1	51,852	25,675	50%
4001879	E/F	1	1,116,165	928,947	83%
4001432	E2	13	609,466	609,466	100%
4002374	E2	13	853,295	356,291	42%
4004574	E4	11	6,410,861	2,351,386	37%
3009581	D1	17	233,524	82,588	35%
3009610	D1	17	1,858,544	1,146,314	62%
3009416	D1	17	293,458	123,453	42%
3009607	D1	17	417,432	376,416	90%
3009915	D1	17	69,204	64,068	93%
4002242	E1	9.2	414,031	116,731	28%
3001535	D		502,491	134,720	27%
3003017	D		551,494	175,705	32%
3002426	D		45,627	-	0%
3001927	D		301,467	183,292	61%
3004641	D		197,637	-	0%
4003316	E4	21	563,320	138,684	25%
"			7,721,199	2,257,506	29%
4004966	E4		155,655	87,684	56%
4002204	E2	9	161,410	39,378	24%
Total			**556,425,075**	**30,952,542**	6%

* Recovery rate = Amount Awarded/Claimed amount.

Annex III: Excerpts of OIOS findings and excerpts of related UNCC comments

Claims category	OIOS assignment no.	Rec no.	OIOS - asserted over compensation (USD)	OIOS assertion *(Excerpted and anonymised by the Board)*	UNCC response *(excerpted and anonymised by the Board)*	Correction made by UNCC	Amount of over compensation remaining after UNCC response
D	AE200011/16/1	103	468 130	OIOS requested that the D1 Panel justify why, in its resolution of two claims, it departed from the D4 (PP) (personal property) methodology that was eventually developed by the Panel.	The D1 Panel objected to the appropriateness of being asked to justify the manner in which it exercised its discretion. Secretariat concurs that the OIOS recommendation is not within scope of audit as defined by OLA, since the responsibility of panels of Commissioners to assess evidence, to make findings of fact and to identify and apply legal and equitable principles are facets of a legal process that is not amenable to audit.	No	Nil
F2	AE2001/16/02	102	13 200 000	OIOS disagreed with the manner in which the Panel considered fixed and variable costs and asserted that costs were over estimated.	As the F2 Panel in its report as only making an "estimate" of costs incurred, it rejected both the OIOS assertions and the ability of OIOS to attempt to substitute its judgement for that of the Panel. According to the OLA opinion, it is the responsibility of the Panel to determine what approach and principles to apply to the resolution of claims, and such decisions were not amenable to audit.	No	Nil
F1	AF2002/27/01	110	7 875 000	OIOS disagreed with F1 Panel's finding concerning the sufficiency of evidence upon which it made its recommendation.	The F1 Panel considered the issue of the sufficiency of the evidence at great length and decided that there was sufficient evidence on which to make its recommendation.	No	Nil
		101	1 932 000	OIOS believed there may be an overlap between the amount the F1 Panel recommended in respect of this claim (for costs of evacuation from Kuwait and Iraq) and the amount recommended by the F2 Panel in respect of emergency humanitarian relief provided by to evacuees.	Given the nature of the approach adopted by the F2 Panel, (i.e., an estimate) it is not possible to establish conclusively whether the amounts awarded overlap. However, all possible checks were conducted to minimize that risk. The F1 Panel made its recommendation on the basis of the evidence before it.	No	Nil
		108	98 000	OIOS asserted that the Panel applied an inappropriate exchange rate.	The Panel noted that while the English version of the contract provided an exchange rate the original version did not. Since the original text was controlling under the contract, the Panel therefore decided to apply the commercial exchange rate in effect at the time. According to the OLA, such decision by the Panel is not amenable to audit.	No	Nil
		105	1 000 000	OIOS disagreed with F1 Panel's findings concerning the directness of loss and sufficiency of evidence.	According to OLA, assessments of directness and sufficiency of evidence are for the Panel to make and are not amenable to audit. The Panel make a downward adjustment to take into account the risk of overstatement.	No	Nil

F3	AF2002/27/3	101	17 563 977	OIOS asserted that six incorrect prices were used in valuing the loss, resulting in over compensation.	In accordance with the instructions of the F3 Panel, the expert consultants sampled the prices provided by the claimant. These six prices were not part of the sample. The sampling did not identify any errors. The claim was adjusted for risk of overstatement by application of the verification and valuation programmes developed by the Panel. To alter the amount of compensation recommended would invalidate the use of the sampling technique approved by the Panel and used throughout the F3 claims programme. According to the OLA opinion, (…) not amenable to audit.	No	Nil
		103	43 900 000	OIOS considered that there were "deficiencies" in the evidence for which the Panel should have made a further adjustment.	According to the OLA opinion, the assessment of evidence is the responsibility of the Panel and is not amenable to audit. The Panel made those adjustments for the risk of overstatement arising from deficiencies in the evidence that it believed were appropriate.	No	Nil
		109	2 300 000	OIOS requested justification for not adjusting for savings in general maintenance costs with respect to ammunition and on adjustment to the compensation if no justification could be provided.	The factual investigation conducted by the Panel indicated that maintenance costs continued and therefore no deduction for savings in maintenance costs was warranted.	No	Nil
		112	3 100 000	OIOS requested justification for not adjusting for savings in general maintenance costs for spare parts and equipment and an adjustment to the compensation if no justification could be provided.	Adjustments for maintenance savings were made by the Panel in respect of both the X and spare parts and equipment, applied against the part of the claim for the missiles alone.	No	Nil
		115	25 000 000	OIOS requested justification for not making a deduction for saved expenses on certain equipment.	Given the particular of the equipment, the Panel made an adjustment for saved maintenance expenditure only where it was satisfied that savings were, or should have been achieved.	No	Nil
		118	14 284 000	OIOS asserted that claims for the same items were made in both this claim and claim no. 5000163.	The expert consultants reviewed the evidence of existence of the items in each claim and advised that there were no duplications. The secretariat believes that there is no evidence to the contrary.	No	Nil
		121	4 168 000	OIOS queried the cost of X used to calculate the Panel's recommendation and requested that the calculation be reviewed.	Computational error. Depreciation was understated by $ 2,084,000, with the result that the recommended award was overstated by $1,719,000.	Will be made.	1,719,000 [1]
	[1] In the course of considering OIOS' recommendations, an understatement of USD 682,000 was noticed by the secretariat and expert consultants. In the result, UNCC stated that the amount recommended for the F3 (3/2) instalment will be reduced from USD 2,103,461, 827 to USD 2,100,909,827.						

		131	3 220 000	OIOS queried whether the Panel recommended certain maintenance costs for compensation, since according to OIOS, maintenance costs are recurring and would have been incurred regardless of Iraq's invasion and occupation of Kuwait.	The secretariat explained that the description of some contracts as "maintenance" contracts is a misnomer. Compensation was only recommended in respect of contracts for repairs and replacement necessary as a direct result of Iraq's invasion and occupation of Kuwait.	No	Nil
		134	4 790 000	OIOS requested the evidence to confirm if the claimant paid certain outstanding money to the vendor. If no evidence OIOS said the recommended compensation should be reviewed.	The secretariat identified the legal principle the Panel adopted and explained why the Panel did not require evidence of payment for items of lost property. Such decision concerning the sufficiency of evidence is for the Panel to make and is not amenable to audit.	No	Nil
		136	3 000 000	OIOS sought clarification as to why the claim was not converted to US dollars for the valuation calculations, with the result that the depreciation adjustment is understated by approximately USD 3 million.	Computational error in the calculation of depreciation with the result that it was understated and the amount recommended was overstated by USD 1,515,000.	Will be made.	1515000 [2]
		141	41 142 000	OIOS disagreed with the Panel's decision concerning the compensability of certain back salary payments to personnel.	According to the OLA opinion (…) are not amenable to audit.	No	Nil
	[2] In the course of considering OIOS' recommendations, an understatement of USD 682,000 was noticed by the secretariat and expert consultants. In the result, the amount recommended for the F3 (3/2) instalment will be reduced from USD 2,103,461, 827 to USD 2,100,909,827.						
E.5	AF2002/27/5	101	225 000	OIOS asserted that Governing Council decision 21 has not been properly applied.	No panels of Commissioners have interpreted decision 21 in the manner that OIOS suggested it be applied. According to the OLA opinion, (…) not amenable to audit.	No	Nil
		103	81 000	OIOS asserted that an adjustment was necessary for compensation already received.	Computational error.	Yes	81,000
		104	20 000	OIOS asserted that in several instances, the amount recommended exceeded the amount claimed.	Computational error.	Yes	20,000
TOTAL AMOUNT audited *(including claims not mentioned in the above selection)*		**655 606 107**					**3 335 000**

Chapter III
Audit opinion

We have audited the accompanying financial statements of the United Nations Compensation Commission, comprising statements numbered I to III and the supporting notes for the biennium ended 31 December 2003. These financial statements are the responsibility of the Secretary General of the United Nations. Our responsibility is to express an opinion on these financial statements based on our audit.

We conducted our audit in accordance with the Common Auditing Standards of the Panel of External Auditors of the United Nations, the specialized agencies and the International Atomic Energy Agency and conforming with International Standards on Auditing. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, and as considered by the auditor to be necessary in the circumstances, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by the Secretary-General, as well as evaluating the overall presentation of the financial statements. We believe that our audit provides a reasonable basis for the audit opinion.

In our opinion, these financial statements present fairly, in all material respects, the financial position as at 31 December 2003 and the results of operations and cash flows for the biennium then ended in accordance with the UNCC's stated accounting policies set out in note 2 of the financial statements, which were applied on a basis consistent with that of the preceding financial period.

Furthermore, in our opinion, the transactions of the United Nations Compensation Commission that have come to our notice or which we have tested as part of our audit have, in all significant respects, been in accordance with the Financial Regulations and Legislative authority.

In accordance with article VII of the Financial Regulations, we have also issued a long-form report on our audit of the financial statements on the United Nations Compensation Commission.

(*Signed*) Shauket A. **Fakie**
Auditor-General of the Republic of South Africa

(*Signed*) Guillermo N. **Carague**
Chairman, Philippine Commission on Audit

(*Signed*) François **Logerot**
First President of the Court of Accounts of France

9 July 2004

Note: The members of the Board of Auditors have signed only the original English version of the audit opinion.

Chapter IV

Certification of the financial statements

1. The financial statements of the United Nations Compensation Commission established pursuant to Security Council resolution 692 (1991) for the biennium 2002-2003 ending 31 December 2003 have been prepared in accordance with financial rule 106.10.

2. The summary of significant accounting policies applied in the preparation of these statements is included as notes to the financial statements. These notes provide additional information and clarifications for the financial activities undertaken by the Commission during the period covered by these statements, for which the Secretary-General has administrative responsibility.

3. Previously, these financial statements were included in Volume I of the United Nations financial statements.

4. I certify that the appended financial statements of the United Nations Compensation Commission, numbered I to III are correct.

(*Signed*) Jean-Pierre **Halbwachs**
Assistant Secretary-General
Controller
25 March 2004

Chapter V

Financial statements for the biennium 2002-2003 ending 31 December 2003

Supplementary information

1. The annex provides information that the Secretary-General is required to report.

Write-off of losses of cash and receivables and property

2. In accordance with financial rules 106.8 and 106.9, there were no losses of cash and receivables and property during the biennium 2002-2003.

Ex-gratia payments

3. There were no ex-gratia payments during the biennium 2002-2003.

Statement I

United Nations Compensation Commission a/

Statement of income and expenditure and changes in reserves and fund balances
for the biennium 2002-2003 ending 31 December 2003
(Thousands of United States dollars)

	2003	2001 b/
Income		
Allocations from other funds c/	3 423 852	8 157 964
Allocations from other organizations d/	196 120	-
Interest income	66 083	182 058
Other/miscellaneous income	580	635
Total income	**3 686 635**	**8 340 657**
Expenditure		
Staff and other personnel costs	77 722	72 282
Travel	554	646
Contractual services	440	644
Operating expenses	8 727	7 443
Acquisitions	285	237
Fellowships, grants, other expenses	6 215	-
Compensation awards	3 656 111	9 532 333
Total expenditure	**3 750 054**	**9 613 585**
Net excess (shortfall) of income over expenditure	**(63 419)**	**(1 272 928)**
Savings on, or cancellation of prior period obligations	74 310	100 653
Other adjustments to fund balances	-	6 000
Reserves and fund balances, beginning of period b/	436 765	1 603 040
Reserves and fund balances, end of period	**447 656**	**436 765**

a/ See note 1.

b/ Comparative figures reclassified to conform to current presentation, see note 3 (a).

c/ From United Nations Escrow Account established under the provisions of Security Council resolution 986 (1995).

d/ Represents 5% of the proceeds from Iraqi oil sales deposited into the Development Fund for Iraq as per Security Council resolution 1483 (2003), see note 1 (c).

The accompanying notes are an integral part of the financial statements.

Statement II

United Nations Compensation Commission a/

Statement of assets, liabilities and reserves and fund balances as at 31 December 2003

(Thousands of United States dollars)

	2003	2001 b/
Assets		
Cash and term deposits	7 385	20 013
Cash pool c/	468 198	1 076 437
Inter-fund balances receivable	-	127 256
Other accounts receivable d/	8 539	6 987
Deferred charges	1 141	5
Total assets	**485 263**	**1 230 698**
Liabilities		
Unliquidated obligations - current period	11 995	728 678
Unliquidated obligations - future periods	1 107	-
Inter-fund balances payable	12 343	-
Other accounts payable e/	12 162	65 255
Total liabilities	**37 607**	**793 933**
Reserves and fund balances		
Operating reserve f/	135 000	140 000
Cumulative surplus	312 656	296 765
Total reserves and fund balances	**447 656**	**436 765**
Total liabilities, reserves and fund balances	**485 263**	**1 230 698**

a/ See note 1.

b/ Comparative figures reclassified to conform to current presentation, see note 3 (a).

c/ Represents share of the United Nations Headquarters Cash Pool and comprises cash and term deposits of $106,934,287, short-term investments of $60,418,586 (market vaule $60,458,282), long-term investments of $299,401,337 (market value $297,159,593) and accrued interest receivable of $1,444,356.

d/ Includes US$8,215,924 paid to governments for further distribution to claimants in respect of various compensation awards.

e/ Includes US$11,953,977 undistributed funds to claimants.

f/ Pursuant to authorization by the Governing Council, an amount of $5,000,000 was transferred from operating reserve for the provision of technical assistance to Iraq in the review of environmental claims.

The accompanying notes are an integral part of the financial statements.

Statement III

United Nations Compensation Commission a/

Statement of cash flows for the biennium 2002-2003 ending 31 December 2003

(Thousands of United States dollars)

	2003	2001 b/
Cash flows from operating activities		
Net excess (shortfall) of income over expenditure (Statement I)	(63 419)	(1 272 928)
(Increase) decrease in other accounts receivable	(1 552)	61 720
(Increase) decrease in deferred charges	(1 136)	(5)
Increase (decrease) in unliquidated obligations	(715 576)	462 795
Increase (decrease) in other accounts payable	(53 093)	(55 534)
Less: interest income	(66 083)	(182 058)
Net cash from operating activities	(900 859)	(986 010)
Cash flows from investing and financing activities		
(Increase) decrease in short-term investments	-	1 094 715
(Increase) decrease in cash pool	608 239	(1 076 437)
(Increase) decrease in inter-fund balances receivable	127 256	120 934
Increase (decrease) in inter-fund balances payable	12 343	-
Plus: interest income	66 083	182 058
Net cash from investing and financing activities	813 921	321 270
Cash flows from other sources		
Savings on or cancellation of, prior period obligations	74 310	100 653
Other adjustments to reserves and fund balances	-	6 000
Net cash from other sources	74 310	106 653
Net increase (decrease) in cash and term deposits	(12 628)	(558 087)
Cash and term deposits, beginning of period	20 013	578 100
Cash and term deposits, end of period c/	7 385	20 013

a/ See note 1.

b/ Comparative figures have been reclassified to conform to current presentation, see note 3 (a).

c/ Cash and term deposits does not include cash and term deposits in the cash pool. Refer footnote c/ in statement II.

The accompanying notes are an integral part of the financial statements.

Notes to the financial statements

Note 1. The United Nations Compensation Commission

(a) The United Nations Compensation Commission (the Commission) was established in 1992 in accordance with Security Council resolution 692 (1991) subsequent to Security Council resolution 687 (1991), to administer the settlement of claims arising from any direct loss, damage, or injury for which the Government of Iraq is held liable as a result of its invasion and occupation of Kuwait.

(b) By its resolution 986 (1995), the Security Council approved the allocation of 30 per cent of the proceeds from sale of Iraqi oil to the Commission. Following Security Council resolution 1330 (2000), the allocation to the Commission was decreased from 30 per cent to 25 per cent effective 6 December 2000.

(c) By its resolution 1483 (2003), the Security Council decided that effective 23 May 2003, all proceeds from the export sales of Iraqi oil shall be deposited into the Development Fund for Iraq (DFI), which is administered by the Coalition Provisional Authority (CPA). The Security Council further approved that 5 per cent of the oil sales proceeds received in the Development Fund for Iraq shall be deposited into the Compensation Fund.

Note 2. Summary of significant accounting and financial reporting policies of the United Nations Compensation Commission

(a) The accounts of the United Nations Compensation Commission are maintained in accordance with the Financial Regulations of the United Nations as adopted by the General Assembly, the rules formulated by the Secretary-General as required under the regulations, and administrative instructions issued by the Under Secretary-General for Management, or the Controller. They also take fully into account the United Nations System Accounting Standards, as adopted by the former Administrative Committee on Coordination (ACC). The ACC has since been replaced by Chief Executives Board for Coordination (CEB). The Commission follows International Accounting Standard 1 – Presentation of Financial Statements, on the disclosure of accounting policies, as modified and adopted by the CEB as shown below:

(i) Going concern, consistency, and accrual are fundamental accounting assumptions. Where fundamental accounting assumptions are followed in financial statements, disclosure of such assumptions is not required. If a fundamental accounting assumption is not followed, that fact should be disclosed together with the reasons;

(ii) Prudence, substance over form, and materiality should govern the selection and application of accounting policies;

(iii) Financial statements should include clear and concise disclosure of all significant accounting policies that have been used;

(iv) The disclosure of the significant accounting policies used should be an integral part of the financial statements. These policies should normally be disclosed in one place;

(v) Financial statements should show comparative figures for the corresponding period of the preceding financial period;

(vi) A change in an accounting policy that has a material effect in the current period or may have a material effect in subsequent periods should be disclosed together with the reasons. The effect of the change should, if material, be disclosed and quantified.

(b) The Commission's accounts are maintained on a "fund accounting" basis.

(c) The financial period of the Commission is a biennium and consists of two consecutive calendar years.

(d) Generally, income, expenditure, assets, and liabilities are recognized on the accrual basis of accounting.

(e) The accounts of the Commission are presented in United States dollars. Accounts maintained in other currencies are translated into United States dollars at the time of the transactions at rates of exchange established by the United Nations. In respect of such currencies, the financial statements reflect the cash, investments and current accounts receivable and payable in currencies other than the United States dollars, translated at the applicable United Nations rates of exchange in effect as at the date of the statements. In the event that the application of actual exchange rates at the date of the statements would provide a valuation materially different from the application of the United Nations rates of exchange for the last month of the financial period, a footnote will be provided quantifying the difference.

(f) The Commission's financial statements are prepared on the historical cost basis of accounting, and are not adjusted to reflect the effects of changing prices for goods and services.

(g) The Cash Flow Summary statement is based on the "Indirect Method" of cash flow as referred to in the United Nations System Accounting Standards.

(h) The Commission's financial statements are presented in accordance with the ongoing recommendations of the Working Party on Accounting Standards to the CEB.

(i) Income:

(i) Allocations from other funds represent monies appropriated or designated from one fund for the transfer to and disbursement from another fund;

(ii) Income received under inter-organization arrangements represents allocations of funding from agencies to enable the Commission to administer projects or other programmes on their behalf;

(iii) Interest income includes all interest earned on deposits in various bank accounts and investment income earned in United Nations cash pool. All realized losses and net unrealized losses on short-term investments are offset against investment income. Investment income and costs associated with operation of investments in the cash pool are allocated to the Commission;

(iv) Miscellaneous income includes income from sale of used or surplus property, refunds of expenditures charged to prior periods, income from net gains resulting from currency translations, settlements of insurance claims, monies accepted for which no purpose was specified, and other sundry income;

(v) Income for future financial periods is not recognized in the current financial period and is recorded as deferred income as referred to in item (l)(iii).

(j) Expenditures:

(i) Expenditures are incurred against authorized allotments. Total expenditures reported include unliquidated obligations and disbursements;

(ii) Expenditures incurred for non-expendable property are charged to the budget of the period when acquired and are not capitalized. Inventory of such non-expendable property is maintained at historical cost;

(iii) Expenditures for future financial periods are not charged to the current financial period and are recorded as deferred charges as referred to in item (k)(v).

(k) Assets:

(i) Cash and term deposits represent funds held in demand deposit accounts and interest-bearing bank deposits;

(ii) Cash pool comprises the Commission's share of cash and term deposits, short-term and long-term investments and accrual of investment income, all of which are managed in the United Nations cash pool. Investments in the cash pool are similar in nature. Short-term

investments are stated at lower of cost or market; long-term investments are stated at cost. Cost is defined as the nominal value plus/minus any unamortized premium/discount. The market value of investments is disclosed in the footnotes to the financial statements;

(iii) Interfund balances reflect transactions between funds, and are included in the amounts due to and from the United Nations General Fund. Interfund balances also reflect transactions directly with the United Nations General Fund. Interfund balances are settled periodically dependent upon availability of cash resources;

(iv) Provision for delays in collection of receivable balances is not made;

(v) Deferred charges normally comprise expenditure items that are not properly chargeable to the current financial period. They will be charged as expenditure in a subsequent period. These expenditure items include commitments approved by the Controller for future financial periods in accordance with financial rule 106.7. Such commitments are normally restricted to administrative requirements of a continuing nature and to contracts or legal obligations where long lead-times are required for delivery;

(vi) For purposes of the balance sheet statements only, those portions of education grant advances that are assumed to pertain to the scholastic years completed as at the date of the financial statement are shown as deferred charges. The full amounts of the advances are maintained as accounts receivable from staff members until the required proofs of entitlement are produced, at which time the budgetary accounts are charged, and the advances settled;

(vii) Maintenance and repairs of capital assets are charged against the appropriate budgetary accounts. Furniture, equipment, other non-expendable property, and leasehold improvements are not included in the assets of the Commission. Such acquisitions are charged against budgetary accounts in the year of purchase. The value of non-expendable property is disclosed in notes to the financial statements.

(l) Liabilities and reserves and fund balances:

(i) Operating reserves are included in the totals for "Reserves and fund balances" shown in the financial statements;

(ii) Unliquidated obligations for future years are reported both as deferred charges and as unliquidated obligations;

(iii) Deferred income includes income received but not yet earned;

(iv) Commitments of the Commission are shown as unliquidated obligations and other accounts payable. Current period obligations remain valid for 12 months following the end of the biennium to which they relate, and other accounts payable includes funds

returned by governments in respect of claimants that could not be located, for a period of upto 24 months from the date of initial payment. At the end of the specified periods, unliquidated obligations and balances in the other accounts payables are cancelled and returned to the Compensation Fund as savings on, or cancellation of prior period obligations;

(v) Contingent liabilities, if any, are disclosed in the notes to the financial statements;

(vi) The United Nations is a member organization participating in the United Nations Joint Staff Pension Fund (UNJSPF), which was established by the United Nations General Assembly to provide retirement, death, disability and related benefits. The UNJSPF is a funded defined benefit plan. The financial obligation of the Commission to the UNJSPF consists of its mandated contribution at the rate established by the United Nations General Assembly together with its share of any actuarial deficiency payments under Article 26 of the Regulations of the UNJSPF. Such deficiency payments are only payable if and when the United Nations General Assembly has invoked the provision of Article 26, following determination that there is a requirement for deficiency payments based on an assessment of the actuarial sufficiency of the UNJSPF as of the valuation date. As at the date of the current financial statement, the United Nations General Assembly has not invoked this provision.

Note 3. Statements I, II and III

(a) Previously the accounting policy was that at the end of a financial period, obligations for compensation awards were raised to the extent of available cash. Effective 1 January 2002, the accounting policy has been changed to discontinue this practice, and obligations raised at the end of previous financial periods have been reversed. Accordingly, comparative figures for expenditures, unliquidated obligations and reserves and fund balances have been revised to conform to the current presentation.

(b) As of 31 December 2003, compensation claims of $30,118,720,590 have been approved by the Governing Council of the Commission but not yet paid nor obligated pending receipt of funds from the Development Fund for Iraq established further to Security Council resolution 1483 (2003).

(c) With respect to awards of interest, the Governing Council of the Commission decided in 1992 that interest would be awarded from the date the loss occurred until the date of payment, at a rate sufficient to compensate successful claimants for the loss of use of the principal amount of the award; that the methods of calculation and of payment of interest would be considered by the Governing Council at the appropriate time; and that interest would be paid after the principal amount of awards. As a decision on awarding the interest has not yet been taken by the Governing Council, it is not possible to estimate the value of such awards of interest.

Note 4. Non-expendable property

In accordance with United Nations accounting policies, non-expendable property is not included in the fixed assets of the Commission but is charged against the current allotment in the year of purchase. The Commission's non-expendable property, valued at historical cost, according to the cumulative inventory records is $2,152,977 as at 31 December 2003.

Note 5. Liabilities for end-of-service benefits

(a) The Commission has not specifically recognized, in any of its financial accounts, liabilities for after-service health insurance (ASHI) costs or the liabilities for other types of end-of-services payments, which will be owed when staff members leave the Commission. Actual payments made in each financial period are reported as current expenditures. In order to gain a better understanding of the financial dimensions of the Commission's liabilities for after-service health insurance, a consulting actuary was engaged to carry out an actuarial valuation of post-retirement benefits. It is estimated that the Commission's liability as at 31 December 2003 is as follows:

After-service health insurance liability	Present value of future benefits	Accrued liability
	(United States dollars)	
Gross liability	659,000	659,000
Offset from retiree contributions	(165,000)	(165,000)
Net Liability	**494,000**	**494,000**

(b) The present value of future benefits figures shown above are the discounted values of all benefits to be paid in the future to all current retirees and active employees expected to retire. The accrued liabilities represent those portions of the present values of benefits that have accrued from the staff members' dates of entry on duty until the valuation date. Active staff members' benefits are fully accrued on the date on which they become fully eligible for benefits.

(c) Staff members who separate from the Commission are entitled to be paid for any unused vacation days they may have accrued up to a maximum limit of 60 days. The Commission's total liability for such unpaid accrued vacation compensation as of 31 December 2003 is estimated at $1.6 million.

(d) Some staff members are entitled to repatriation grants and related expenditures of relocation upon their termination from the Commission based on the number of years of service. The Commission's total liability for such unpaid repatriation and relocation entitlement as of 31 December 2003 is estimated at $3.1 million.

(e) Some staff members are entitled to a termination indemnity should the Commission terminate their appointments. The Commission's liability for such costs as of 31 December 2003 is estimated to be not in excess of $5.0 million.